FINANCIAL STATEMENTS,
REQUIRED SUPPLEMENTARY INFORMATION
AND SUPPLEMENTAL SCHEDULES

Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)
Year Ended June 30, 2015
With Report of Independent Auditors
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Financial Statements, Required Supplementary Information  
and Supplemental Schedules  

Year Ended June 30, 2015  

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Financial Section
Report of Independent Auditors

To the Governing Board of the
Puerto Rico Electric Power Authority

Report on the Financial Statements

We have audited the accompanying financial statements of Puerto Rico Electric Power Authority (the “Authority” or “PREPA”), a component unit of the Commonwealth of Puerto Rico as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the Authority’s basic financial statements as listed in the table of contents.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of PREPA Holdings LLC (a blended component unit), which statements reflect total assets constituting 0.6%, and total revenues constituting 0.5% of the related combined totals. Those financial statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for PREPA Holdings, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States, 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 of material misstatement.

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

**Basis for Qualified Opinion**

As described in Note 2 to the basic financial statements, the Authority has implemented Statement No. 68 of the Governmental Accounting Standard Board, *Accounting and Financial Reporting for Pensions*, and GASB Statement No. 71, *Pension Transition for contributions Made subsequent to the Measurement Date*, an amendment of GASB Statement No. 68. As part of this implementation, the actuarial valuation used by the Authority incorrectly considered actual instead of projected investment returns for certain periods subsequent to the measurement date in the calculation of its discount rate assumption used to estimate the net pension liability. Such error resulted in an overstatement of the net pension liability for the Authority as of June 30, 2015, by an estimated amount ranging from approximately $76 million to $194 million, depending on the discount rate assumption ultimately used.

**Qualified Opinion**

In our opinion, based on our audit and the report of the other auditors, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the Puerto Rico Electric Power Authority as of June 30, 2015, and the changes in its financial position and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

**The Authority’s Ability to Continue as a Going Concern**

The accompanying financial statements have been prepared assuming that the Authority will continue as a going concern. As discussed in Note 19 to the financial statements, the Authority does not have sufficient funds available to fully repay its various obligations as they come due and has entered a process to restructure its long-term debt. The financial difficulties experienced by the Authority, including the uncertainty as to its ability to fully satisfy its obligations, raises substantial doubt about its ability to continue as a going concern. Management’s plans in regard to these matters are also described in Notes 19 and 20. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.
Adoption of GASB Statement No. 68, Accounting and Financial Reporting for Pensions and GASB 71, Pension Transition for Contributions Made Subsequent to the Measurement Date

As described in Note 18 to the financial statements, the Puerto Rico Electric Power Authority adjusted its financial statements as a result of the adoption of Government Auditing Standards Board (GASB) Statement No. 68, Accounting and Financial Reporting for Pensions and GASB 71, Pension Transition for Contributions Made Subsequent to the Measurement Date, effective July 1, 2014. Our opinion is not modified with respect to this matter.

Required Supplementary Information

U.S. generally accepted accounting principles require that management’s discussion and analysis on pages 4 through 18 and the Supplementary Schedule of Funding Progress-Postemployment Health Plan, Schedule of Changes in the Authority’s Net Pension Liability and Related Ratios and Schedule of Employer Contributions on pages 136 through 139, respectively, 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 which 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, 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.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Puerto Rico Electric Power Authority’s basic financial statements. The supplemental schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements.

The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information 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 April 20, 2018 on our consideration of the Authority’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 the effectiveness of the Authority’s internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Authority’s internal control over financial reporting and compliance.

April 20, 2018

Stamp No. E318302
affixed to
original of
this report.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Management’s Discussion and Analysis  
(Unaudited)  
Year Ended June 30, 2015

Introduction

The Puerto Rico Electric Power Authority ("the Authority") was created in 1941 as a public corporation and governmental instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth") by Act No. 83 of the Legislative Assembly of Puerto Rico, approved May 2, 1941, as amended. The Authority is one of the largest municipal utilities in the United States, ranking first in the number of customers and revenues among public power utilities for calendar year 2014.

As of June 30, 2015, the total nameplate rating of the Authority-owned generating facilities was 4,938 megawatts "MW" and their total dependable generating capacity was 4,878 MW. In addition, the Authority has the right to purchase up to 961 MW of power under long term purchase agreements from two co-generation facilities.

The Authority’s transmission and distribution system interconnects its power plants with major switching and load centers throughout Puerto Rico in order to allow the flow of power to and between these locations. The electric system is integrated, and each generating unit is able to provide electric power to the transmission and distribution system.

This section of the financial report presents the analysis of the Authority’s financial performance during the fiscal years ended June 30, 2015 and 2014. We recommend readers to consider the information herein presented in conjunction with the financial statements that follow this section.

Financial Highlights

- Operating (loss)income for fiscal years ended June 30, 2015 and 2014 was $(323.1) million and $223.5 million respectively, representing a decrease of $546.6 million or (244.6) percent.

- Operating expenses increased by $(56.4) million or (1.3) percent, from $4.2 billion in 2014 to $4.2 billion in 2015.

- Net Utility Plant for the fiscal year ended June 30, 2015 decreased by $148 million or 2.2 percent, which represents the net of additions for $217 million and net depreciation of $366 million.
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Management’s Discussion and Analysis  
(Unaudited)  
Year Ended June 30, 2015

- Total assets and deferred outflows of resources increased by $1,138.9 million or 10.9 percent for the fiscal year ended June 30, 2015.

- For the fiscal year ended June 30, 2015, as compared to the fiscal year ended June 30, 2014, current accounts receivable net increased by 35.3 percent from $1,500.5 million to $2,030.6 million. Noncurrent portion of account receivable net, decreased by 37.8 percent from $120.0 million to $74.6 million.

- Accounts receivable from the governmental sector increased 112.4 percent from $803.7 million on June 30, 2014 to $1,707 million on June 30, 2015, of which $31.4 million and $83.8 million was reserved for uncollectibility, respectively.

- Fuel adjustment revenues were $2,129.8 million for the fiscal year ended June 30, 2015 and $2,633 million for the fiscal year ended June 30, 2014, representing a decrease of $503.4 million between fiscal years 2014 and 2015. Fuel expenses were $1,887 million for fiscal year 2015 and $2,345 million for fiscal year 2014, representing a decrease of $458 million between fiscal years 2014 and 2015. The decreases in the fuel adjustment revenues and fuel expenses for fiscal year 2015, as compared to 2014, were mainly due to a decrease in the average fuel oil price per barrel of $21.06 (24.6%) net of an increase of 135,700 barrels of fuel consumption.

- Purchased power adjustment revenues were $884.2 million for fiscal year 2015 and $904 million for fiscal year 2014, representing a decrease of $19.8 million between fiscal years 2014 and 2015. Purchased power adjustment expenses were $789.7 million for fiscal year 2015 and $807.6 million for fiscal year 2015, representing a decrease of $17.9 million between fiscal years 2014 and 2015. The decrease in the purchased power adjustment revenues and expenses was due to a decrease of price per kilowatt hour ("kWh") of purchased power by one-half of a cent (or 4.3%) for fiscal year 2015 as compared to fiscal year 2014.

Overview of Financial Report

Management’s Discussion and Analysis (MD&A) of operating results serves as an introduction to the basic financial statements and supplementary information. Summary financial statement data, key financial and operational indicators used in the Authority’s strategic plan, projected capital improvement program, operational budget and other management tools were used for this analysis.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Management's Discussion and Analysis  
(Unaudited)  
Year Ended June 30, 2015  

Required Financial Statements  

The financial statements report the financial position and operations of the Authority and its blended component units, Puerto Rico Irrigation Systems and PREPA Holdings LLC as of and for the year ended June 30, 2015, which include a Statement of Net Position, Statement of Revenues, Expenses and Changes in Net Position, Statement of Cash Flows and the notes to financial statements.  

The Statement of Net Position presents the financial position of the Authority and provides information about the nature and amount of resources and obligations at year-end.  

The Statement of Revenues, Expenses and Changes in Net Position presents the results of the business activities over the course of the fiscal year and information as to how Authority's net position changed during the fiscal year.  

The Statement of Cash Flows shows changes in cash and cash equivalents, resulting from operating, non-capital and capital financing, and investing activities, which include cash receipts and cash disbursement information, without consideration of the depreciation of capital assets and other non-cash items.  

The notes to the financial statements provide information required and necessary to the understanding of material information of the Authority's financial statements. These notes present information about the Authority's significant accounting principles, significant account balances and activities, risk management, obligations, commitments and contingencies, and subsequent events.  

Financial Analysis  

Our analysis below focuses on the Authority's net position/(deficit) and changes in net position/(deficit) during the year.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico) 

Management’s Discussion and Analysis  
(Unaudited)  
Year Ended June 30, 2015 

Authority’s Net Position  
(In thousands) 

<table>
<thead>
<tr>
<th></th>
<th>Year Ended June 30, 2015</th>
<th>2014 (as previously reported)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current, non-current and other assets</td>
<td>$3,248,644</td>
<td>$3,504,903</td>
</tr>
<tr>
<td>Deferred outflows of resources</td>
<td>1,670,065</td>
<td>126,812</td>
</tr>
<tr>
<td>Capital assets</td>
<td>6,699,345</td>
<td>6,847,456</td>
</tr>
<tr>
<td>Total assets and deferred outflows of resources</td>
<td>$11,618,054</td>
<td>$10,479,171</td>
</tr>
<tr>
<td>Long-term debt outstanding</td>
<td>$9,203,248</td>
<td>$9,413,195</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>6,412,043</td>
<td>2,332,981</td>
</tr>
<tr>
<td>Deferred inflows of resources</td>
<td>57,703</td>
<td>-</td>
</tr>
<tr>
<td>Total liabilities and deferred inflows of resources</td>
<td>$15,672,994</td>
<td>$11,746,176</td>
</tr>
<tr>
<td><strong>Net position (deficit):</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net investments in capital assets</td>
<td>($1,017,787)</td>
<td>($253,448)</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>($3,037,153)</td>
<td>($1,013,557)</td>
</tr>
<tr>
<td>Total net position (deficit)</td>
<td>($4,054,940)</td>
<td>($1,267,005)</td>
</tr>
</tbody>
</table>

A portion of the Authority’s net deficit reflects its net investment in capital assets, which increased from $(253) million to $(1,018) million as of June 30, 2015.

Changes in the Authority’s net deficit can be determined by reviewing the following condensed Statements of Revenues, Expenses and Changes in Net Position.
## Authority's Changes in Net Position
(In thousands)

<table>
<thead>
<tr>
<th></th>
<th>Year Ended June 30, 2015</th>
<th>2014 (as previously reported)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating revenues</td>
<td>$ 3,865,458</td>
<td>$ 4,468,922</td>
</tr>
<tr>
<td>Other income</td>
<td>44,263</td>
<td>21,157</td>
</tr>
<tr>
<td>Total revenues</td>
<td>3,909,721</td>
<td>4,490,079</td>
</tr>
<tr>
<td>Operating expenses</td>
<td>4,188,604</td>
<td>4,245,892</td>
</tr>
<tr>
<td>Non-operating expenses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest expense, net</td>
<td>468,278</td>
<td>431,180</td>
</tr>
<tr>
<td>Impairment loss on GDB deposits</td>
<td>144,733</td>
<td>-</td>
</tr>
<tr>
<td>Total Non-operating expenses</td>
<td>613,011</td>
<td>431,180</td>
</tr>
<tr>
<td>Total expenses</td>
<td>4,801,615</td>
<td>4,677,072</td>
</tr>
<tr>
<td>Loss before contribution in lieu of taxes and capital contributions</td>
<td>(891,894)</td>
<td>(186,993)</td>
</tr>
<tr>
<td>Contribution in lieu of taxes and other</td>
<td>(273,460)</td>
<td>(277,776)</td>
</tr>
<tr>
<td>Loss before capital contributions</td>
<td>(1,165,354)</td>
<td>(464,769)</td>
</tr>
<tr>
<td>Capital contributions</td>
<td>21,404</td>
<td>44,959</td>
</tr>
<tr>
<td>Change in net position</td>
<td>(1,143,950)</td>
<td>(419,810)</td>
</tr>
<tr>
<td>Net position (deficit) at beginning of year</td>
<td>(1,267,005)</td>
<td>(847,195)</td>
</tr>
<tr>
<td>Cumulative effect of a change in accounting principle for pension costs</td>
<td>(1,643,985)</td>
<td>-</td>
</tr>
<tr>
<td>Net position (deficit) as restated</td>
<td>(2,910,990)</td>
<td>(847,195)</td>
</tr>
<tr>
<td>Net position (deficit) at end of year</td>
<td>$(4,054,940)</td>
<td>$(1,267,005)</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)

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Change in Net Position Analysis

For fiscal year ended June 30, 2015, as compared to June 30, 2014, net deficit increased by $2,788 million.

The cumulative effect of a change in accounting for pension costs in beginning net position was due to the implementation of GASB 68, Accounting and Financial Reporting for Pensions, Accounting and Financial Reporting for Pensions, and GASB 71, Pension Transition for Contributions Made Subsequent to the Measurement Date, which caused the Authority to recognize a net pension liability of $1,644 million. Net position(deficit) decreased by $1,144 million for the year ended in June 30, 2015, which represents a $724 million decrease when compared to the $420 million net position(deficit) decrease for fiscal year ended in June 30, 2014. The reduction in net position(deficit) was driven by the decrease in (i) operating revenues of $603.5 million, mainly due to: a decrease in energy sales per kWh from 17.6 billion in 2014 to 17.3 billion in 2015 (1.7%), representing a $439 million decrease; an increase in the reserve for uncollectible accounts of $218.1 million during the fiscal year 2015, due to a change in the assumptions related to customer collections and the reserve for uncollectible accounts, where management decided to reserve accounts receivables with balances due for over two years, as a result of the recent economic situation facing Puerto Rico; and (ii) a net increase in operating expenses of $(57.3) million, mainly resulting from the lower cost of fuel prices and (iii) an impairment loss of $144.7 million was recognized on the Authority’s deposits at the Puerto Rico Governmental Development Bank (“GDB”), as result of executive orders OE-2016-010 and OE-2016-014, each issued pursuant to Act. No 21 of April 6, 2016, also known as the Puerto Rico Emergency Moratorium and Rehabilitation Act (the “Moratorium Act”), as extended by OE-2017-31, each as described more fully in Note 20 - Subsequent Events.

For fiscal year ended June 30, 2014, as compared to June 30, 2013, net position decreased by $419.8 million, a $147.7 million decrease when compared to the decrease for fiscal year ended June 30, 2013. The reduction in net position was mainly due to a combination of factors that included, among others, a decrease in operating revenues of $374.1 million, mainly due to a decrease in energy sales per kWh from 18.2 million in 2013 to 17.6 million in 2014 (3.3%), representing a $16.8 million basic revenue decrease, and an increase in the reserve for uncollectible accounts of $191.5 million during the fiscal year 2014, due to a change in the assumptions related to collections, as a result of the recent economic situation facing Puerto Rico, net of a decrease in operating expenses of $243.1 million, mainly as a result of a decrease in fuel prices.
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Capital Assets and Debt Administration  

Net Investment in Capital Assets  

Net investment in capital assets as of June 30, 2015 and 2014, amounted to approximately $6,699 million, and $6,847 million (net of accumulated depreciation), respectively. This net investment in capital assets includes land, generation, transmission and distribution systems, buildings, fixed equipment, furniture, fixtures and equipment. The Authority’s net investment in capital assets decreased by 2.2 percent and increased by 1.3 percent for years ended June 30, 2015 and 2014, respectively.  

A substantial portion of the capital expenditures for production plant in fiscal years ended June 30, 2015 and 2014 was spent on the rehabilitation and life extension of generating plants in order to maintain availability, reliability and efficiency.  

Major capital assets projects undertaken by Authority during fiscal years 2015 and 2014 included the following:  

- The Authority performed scheduled maintenance activities for the boilers of Units 1 and 2 of Aguirre Steam Plant. After the natural gas conversion of Costa Sur Steam Plant Units 5 and 6 during the fiscal year ended June 30, 2013, the Authority began the evaluation process for the conversion of Aguirre units to natural gas. The first unit scheduled for conversion will be Unit 1, beginning in second semester of the fiscal year ending June 30, 2018, followed by Unit 2 in first semester of the fiscal year ending June 30, 2019. Improvements include the retrofits to boiler’s internal components to burn 100% of natural gas. Once completed, this project will add 900 MW of generating capacity due to the boiler’s dual-firing capabilities that will allow it to burn both natural gas and coal. Additional evaluations for the gas conversion of other units in the Authority’s fleet are still pending since the new Puerto Rico Energy Commission is evaluating the Integrated Resources Planning document filed by the Authority during the fiscal year ended June 30, 2017.  

- During the year ended June 30, 2015, most of the capital expenditures have been targeted to scheduled maintenance projects of its steam unit fleet, combined-cycle units and combustion turbine peaking units. Most of the expenses have been for boilers and turbine-generators. Likewise, balance-of-plant projects are becoming a priority since these systems
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Management’s Discussion and Analysis  
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Year Ended June 30, 2015

provide safe and reliable operation. Long-term service agreements stand for most of the expense related to combined-cycle projects such as San Juan Combined Cycle Plant Units 5 and 6.

• The Authority has important projects for the supply of water for industrial processes and generation. The new demineralized water plant at the Costa Sur Power Plant, as well as Aguirre Power Plant water supply project are examples of key capital improvements focused on reliability and natural resource protection.

• Water infrastructure projects in order to comply with the current and future National Pollutant Discharge Elimination System (NPDES) permits at San Juan Power Plant and Aguirre Power Complex. The integration of advanced water treatment technologies for reusing processed wastewater will benefit the surrounding environment and reduce the processed water with the exception of the non-contact cooling water discharge. In addition, the Aguirre Water Supply Project will substitute the underground water extraction from Southern Aquifer—which is currently experiencing salt infiltration—to a superficial water supply from the Patillas Irrigation Channel, which will provide a fresh water supply to a deteriorated black mangrove area in Jobos Bay for restoration. The expected completion date for the Aguirre Water Supply Project is October 2018. The San Juan Power Plant Project will reuse the processed wastewater of two main outfalls. Phase I, which included the reuse of the feed water heater condensation, was completed in April 2016. Phase IV, which includes the integration of microfiltration and reverse Osmosis treatment technologies, is under the contract signing process. The “in service” date for the San Juan Power Plant Project is expected to occur during the first quarter of calendar year 2018.

• New Reverse Osmosis (“RO”) and Electrode ionization (“EDI”) System installed at South Coast Power Plant during the fiscal year ended June 30, 2015 is currently in service and is providing high reliability and water quality assurance to the Authority's only natural gas burning power plant.

• In January 2016, the Authority commissioned and energized a new 230 kilovolt (“kV”) transmission line stretching 38 miles between the South Coast Steam Plant and the Cambalache Gas Turbines Plant's switchyard, including the corresponding 230 kV terminals and switchyard extensions. The first stage of this project included the
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reconstruction and conversion to 230 kV of an existing 115 kV transmission line between the South Coast Steam Plant and Dos Bocas Hydroelectric Power Plant. The second stage of the project included the construction of a new 230 kV line from Dos Bocas to the Cambalache facilities. The estimated expenditures were $6 million during the fiscal year ended June 30, 2015. This project enhances the reliability and security margins of the transmission by providing an additional interconnection while also increasing the power transfer capability from the south of Puerto Rico to major load centers in the northern and western regions of the island.

- The reconstruction and rehabilitation of 115 kV and 38 kV circuit lines throughout the whole island. This project includes the reconstruction of 42 miles 115 kV transmission line (36100) interconnecting the Bayamon Transmission Center (TC), Cana 115 kV switchyard, Barrio Piñas 115 kV switchyard, Dos Bocas Hydroelectric Plant, and important substations in the municipalities of Bayamon, Toa Baja, Toa Alta, Corozal, Morovis and Ciales. This project consists of seven phases, of which the first two have been completed and are in service. The first phase was the reconstruction of 3.7 miles of 115 kV transmission line with a 556.5 kcmil ACSR conductor from Piñas Switchyard to the Monterrey Substation, completed in April 2014. The second phase was the reconstruction of 3.7 miles of 115 kV transmission line with a 556.5 kcmil ACSR conductor from Monterrey Substation to the Unibon Substation, in service since October 2015. The third phase is the reconstruction of 6.5 miles of 115 kV transmission line with an 1192.5 kcmil ACSR conductor from Bayamon TC to the Cana TC. By the end of the fiscal year ended June 30, 2017, 76% of the third phase was completed. Due to system problems to authorize the corresponding line clearances, this phase has been delayed, and is currently expected to be in service by December 2018. The fourth phase is the reconstruction of three miles of 115 kV transmission line with a 1,192.5 kcmil ACSR conductor from Cana TC to the Piñas Switchyard. As of the end of the fiscal year ended June 30, 2017, 48% of the fourth phase was completed. Because the project depends heavily upon the availability of line clearances, the expected in service date is the same as the third phase (December 2018). The fifth phase is the reconstruction of 4.7 miles of 115 kV transmission line with a 556.5 kcmil ACSR conductor from Unibon Substation to the Morovis Substation, which currently has an expected in service date of December 2019. The sixth phase is the reconstruction of 3.9 miles of 115 kV transmission line with a 556.5 kcmil ACSR conductor from Morovis to the Ciales Substation, which currently has an expected in service date of December 2020. The seventh phase is the reconstruction of 17 miles of 115
Puerto Rico Electric Power Authority
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Year Ended June 30, 2015

kV transmission line with a 556.5 kcmil ACSR conductor from Ciales Substation to the Dos Bocas Hydroelectric Plant, which currently has an expected in service date during the fiscal year ending June 30, 2024. During the fiscal year ended June 30, 2015, the total capital expenditures related to the reconstruction of transmission line 36100 were $20.9 million. The reconstruction and rehabilitation of four 115 kV transmission lines interconnecting the Palo Seco power plant with relevant 115/38 kV transmission centers located in the metropolitan area are also included, with an expected in service date during the fiscal year ending June 30, 2022. Subtransmission circuits interconnecting substations in the municipalities of Orocovis, Barranquitas, Comerío, Arecibo, Utuado, San Sebastián, Lares, Maricao, Las Marias and Mayagüez, located in the central and west regions of the island, are also part of this major reconstruction and rehabilitation plan.

- A new air insulated 115/38 kV transmission center, commissioned and energized in August 2016 in the municipality of Barranquitas significantly improves the reliability and efficiency of the transmission and sub-transmission system of the central mountainous area of PR. The integration of the existing 39000 transmission line and the new 115/38 kV transformer to the sub-transmission system of the area increased the power transfer capability and improved the voltage regulation of the sub-transmission system in Barranquitas, Orocovis, Comerio and nearby municipalities under normal conditions and during contingency situations. The construction of the new Barranquitas transmission center is also being complemented by the reconstruction of the sub-transmission line 6500 ($6 million during FY 2014-15) and the construction of additional new 38 kV lines. The reconstruction of the sub-transmission line 6500 between Barranquitas TC and Orocovis is expected to be completed by May 2018. In addition to the sub-transmission lines to be reconstructed in this area of the central region, major reconstruction projects of aerial 38 kV lines such as the sub-transmission line 2200 that interconnects the transmission center in Cambalache with the Dos Bocas switchyard and lines 1500 and 2000 in the mountainous western part of the Island will significantly improve the reliability of the sub-transmission system in the municipalities of Utuado, Las Marias, Maricao and areas of Mayaguez. The scope of these reconstruction projects includes the replacement of structures, the installation of new overhead phase and ground conductors, new foundations, insulation systems, guyed systems and mechanical hardware.
The Program to improve the subtransmission system at the metropolitan area also continues, including the switchyard extension of the Centro Médico 38 kV Sectionalizer as well as the construction and extension of underground 38 kV lines in the zone of the Medical Center of Puerto Rico. These projects will provide for the integration of an additional 38 kV circuit that will directly interconnect the Centro Médico 38 kV Sectionalizer to critical hospitals and medical research centers in the zone. The reliability of the electric service to critical loads such as the Children’s Hospital, Cardiovascular Center, University Hospital and the School of Medical Sciences will be significantly increased. These sub-transmission projects are expected to be in service during the fiscal year ending June 30, 2021.

During the fiscal year ended June 30, 2015, there were two additional air insulated 115/38 kV transmission centers under construction in the municipalities of San Juan and Caguas. The Buen Pastor Transmission Center, which is expected to be completed in December 2017, will improve the reliability of the commercial and industrial loads in Río Piedras under contingency situations in the southern metropolitan area. The Bairoa Transmission Center, which is expected to be completed in June 2019, will significantly improve the reliability at Caguas and nearby municipalities, by providing backup to 115/38 kV transformer contingencies located at the Caguas Transmission Center. This project has been affected by major delays related to the right of way acquisition of the 115 kV lines that will interconnect the new switchyard to the transmission system. Additional projects are planned to increase the power transfer capability from the 115 kV transmission systems to the sub-transmission system as well as system reliability by adding transformation capacity in existing switchyards such as San Juan Steam Plant and Bayamón TC.

San Juan GIS 38 kV and 115 kV switchgears are expected to enter into service in fiscal years 2017-18 and 2021-22 respectively. This will be one of the Authority’s major gas insulated 115/38 kV switchyards with direct interconnection to the 115 kV metro underground loop. The new GIS switchgears will also provide interconnection to the second 115/38 kV transformer. It will also provide, through the interconnection of the existing air insulated 115 kV bus with the new GIS bus, for the electrical integration of the San Juan Combined Cycle Units 5 and 6 to the 115 kV underground system. These combined cycle units are essential to the system stability of the grid of Puerto Rico.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Management’s Discussion and Analysis  
(Unaudited)  
Year Ended June 30, 2015

• During the fiscal year ended June 30, 2015, the Authority invested $2.4 million in the construction of a new distribution substation in Caparra. This investment included the installation of a new 38/13.2 kV distribution substation with a maximum capacity of 22.4 MVA. This substation improves the reliability of the distribution system in the Guaynabo municipality and increases the capacity of the distribution system to absorb new loads. This project is currently in the commissioning phase and is expected to be energized during the fiscal year ending June 30, 2018.

• During the fiscal year ended June 30, 2015, the Authority also invested $1.8 million in the construction of a new distribution substation in Añasco. This investment included the installation of a 115/13.2 kV distribution substation with a maximum capacity of 22.4 MVA. This substation improves the reliability of the distribution system in the Mayagüez and Añasco municipalities, and increases the capacity of the distribution system to absorb new loads. This project is currently in the commissioning phase and is expected to be energized during the fiscal year ending June 30, 2018.

Additional information on the Authority’s capital assets can be found in Note 6 to the financial statements.

*Long-Term Debt*

At the end of the fiscal years 2015 and 2014, the Authority had total debt outstanding of $9,203.2 million and $9,413.2 million, respectively, comprised of revenue bonds and notes payable.

**Authority’s Outstanding Debt**  
*(In thousands)*

<table>
<thead>
<tr>
<th></th>
<th>2015</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Power revenue bonds, net</td>
<td>$8,448,926</td>
<td>$8,668,425</td>
</tr>
<tr>
<td>Notes payable</td>
<td>754,322</td>
<td>744,770</td>
</tr>
<tr>
<td>Current portion</td>
<td>9,203,248</td>
<td>9,413,195</td>
</tr>
<tr>
<td>(1,183,106)</td>
<td>(1,166,189)</td>
<td></td>
</tr>
<tr>
<td>Long-term debt, excluding current portion</td>
<td>$8,020,142</td>
<td>$8,247,006</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Management’s Discussion and Analysis  
(UNaudited)  
Year Ended June 30, 2015

As of April 20, 2018, the Authority’s bond were rated "Ca" by Moody’s, "D" by S&P and “D” by Fitch. Additional information on the Authority’s long-term debt can be found in Notes 8 and 11 to the financial statements.

Economic Factors and Next Year’s Budgets and Rates

In the last five calendar years, Puerto Rico’s economy has behaved differently than the United States economy in terms of annual Gross Domestic Product (“GDP”). As published by the Bureau of Economic Analysis (“BEA”), the real GDP adjusted for price changes in the third and fourth quarters of calendar year 2014 and for the first and second of calendar year 2015 increased at an annual rate of 1.3%, 0.50%, 0.80% and 0.68%, respectively. The Puerto Rico Planning Board (“PRPB”) is the local government agency that gathers and studies the official economic data. In Puerto Rico, the economy is measured by the Gross National Product (“GNP”). Puerto Rico’s economy (as measured by GNP) declined by 0.1%, 1.8%, and 0.7% during the fiscal years ending June 30, 2013, June 30, 2014, and June 30, 2015, respectively. The GNP provided by the Interamerican University Global Insight (IUGI) in May 2014 estimated GNP decreases of 1.6% and 0.83% for the fiscal years ended June 30, 2014 and June 30, 2015, respectively.

The Authority adopted the 2015 fiscal year budget on October 9, 2014. The same budget was used for the fiscal year ended June 30, 2016. Under the budget for the fiscal year ended June 30, 2015, total revenues were projected to be approximately $4,630 million. In addition, the budget included approximately $245 million of investments in the Capital Improvement Program.

Currently Known Facts or Conditions That May Have a Significant Effect on the Authority’s Financial Condition or Results of Operations

Operational Improvements

The Authority has made significant investments in evaluating and implementing various operational improvements and strategies in an effort to address its ongoing financial challenges. The Authority reduced its number of employees through a combination of attrition from voluntary retirement and the elimination of temporary and vacant positions. In addition, the Authority continues to enforce the new employee hiring freeze implemented in January 2009.
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Management’s Discussion and Analysis
(Unaudited)
Year Ended June 30, 2015

On September 4, 2014, the Authority appointed a chief restructuring officer whose mandate included providing overall leadership to the Authority’s restructuring process, developing a business plan, implementing revenue improvement and cost reduction plans, overseeing and implementing cash and liquidity management activities, improving the Authority’s ability to analyze, track and collect accounts receivable, improving the Authority’s capital expenditure plan, and developing plans to improve the Authority’s generation, transmission, distribution and other operations. The chief restructuring officer resigned on February 1, 2017 and has not been replaced. The process of identifying and implementing operational improvements continues under the direction of the Governing Board.

The Authority’s Management

Under Puerto Rico law, the Governing Board of the Authority is charged with leading the strategic management of the Authority’s operations, including appointing the Executive Director of the Authority and creating and defining the officer roles. On June 26, 2017, Governor Rosselló Nevarez signed into law Act 37-2017 in order to overhaul the Authority’s then-existing governing board structure. Since the enactment of Act 37-2017, the Authority’s Governing Board consists of seven members. Of its seven-member board, six members are designated by the Governor (three of which require Senate approval) and one member will be an elected consumer representative. The members of the Governing Board bring substantial and relevant experience to the Authority’s operations and transformation, including experience leading complex organizations through business and operational changes, the modernization and transformation of utilities; and the identification and deployment of cutting edge energy technologies, renewables and other energy solutions. The Governing Board members also have substantial engineering experience in the areas of generation, transmission and distribution.

In March of 2017, Governor Ricardo Rosselló Nevarez recommended engineer Ricardo L. Ramos to replace the Authority’s Executive Director Javier Quintana.

On November 17, 2017, Mr. Ramos submitted his resignation to the Authority’s Governing Board, and it was made effective immediately. That same day, Governor Ricardo Rosselló Nevarez recommended the appointment of engineer Justo Gonzalez as the interim director of the Authority, while the Governing Board begins the search for Mr. Ramos’ replacement.

On December 1, 2017, the Authority announced the hiring of Todd W. Filsinger of Filsinger Energy Partners as its chief financial advisor to lead the Authority’s restructuring process. Filsinger, who will report directly to the Authority’s Governing Board, will have broad
responsibilities for the financial aspects of operations and will lead the operational and transformational restructuring. Filsinger’s responsibilities at the Authority will involve: (i) independent financial oversight, development of budgets and approval of expenditures; (ii) development and implementation of operational reforms; (iii) development of restructuring, fiscal and transformation plans within the pending Title III proceeding; (iv) implementation of any approved transformation plan and/or certified fiscal plan; addressing issues related to federal funding, compliance, grants and reimbursements; (v) communicating with stakeholders including creditors, the Puerto Rico government, and the Oversight board; and (vi) such other duties as agreed to by the Governing Board and Filsinger.

On March 20, 2018, the Governing Board announced the hiring of Mr. Walter Higgins III as the Authority’s Chief Executive Officer, the first ever non-political appointment of the CEO.

For a discussion of facts and conditions related to the Authority’s liquidity that will have a significant effect on the Authority’s financial condition and operations, see Note 19 (Financial Condition and Liquidity) to the Authority’s financial statements for the fiscal year ended June 30, 2015.

For a discussion of subsequent events that will have a significant effect on the Authority’s financial condition and operations, see Note 20 (Subsequent Events) to the Authority’s financial statements for the fiscal year ended June 30, 2015.

**Request for Information**

This financial report is designed to provide a general overview of the Authority’s finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Authority’s Chief Financial Officer. The executive offices of the Authority are located at 1110 Ponce de León Avenue, San Juan, Puerto Rico 00907 or obtain financial information through the Authority’s official web page www.aeepr.com.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Statement of Net Position  
(In thousands)  

As of June 30, 2015  

**Assets**  
Current assets:  
- Cash and cash equivalents, net $264,653  
- Receivables, net 2,030,617  
- Fuel oil, at average cost 120,314  
- Materials and supplies, at average cost 178,904  
- Prepayments and other assets 3,928  
Total current assets 2,598,416  

Other non-current receivables, net 74,647  

Restricted assets:  
- Investments held by trustee 390,781  
- Construction fund and other special funds 156,221  
Total restricted assets 547,002  

Capital assets:  
- Plant in service 12,815,745  
- Accumulated depreciation (6,787,733)  
Construction in progress 671,333  
Total capital assets, net 6,699,345  

Other assets 28,579  
Total assets 9,947,989  

**Deferred outflows of resources**  
Accumulated decrease in fair value of hedging derivatives 51,195  
Deferred outflows related to pensions 1,552,516  
Deferred loss resulting from debt refunding 66,354  
Total deferred outflows of resources 1,670,065  
Total assets and deferred outflows of resources $11,618,054  

(continued)
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)

Statement of Net Position  
(*In thousands*)

As of June 30, 2015

**Liabilities and Net Position**

**Currents liabilities:**
- Notes payable $733,852
- Accounts payable and accrued liabilities 2,140,966
- Customers’ deposits 14,551
- **Total current liabilities** 2,889,369

**Current liabilities payable from restricted assets:**
- Current portion of long-term debt 449,254
- Accrued interest 211,193
- **Total current liabilities payable from restricted assets** 698,148

**Noncurrent liabilities:**
- Long-term debt, excluding current portion 8,020,142
- Fair value of derivative instruments - interest, basis and commodity swaps 51,195
- Customers’ deposits excluding current portion 171,396
- Net Pension Liability 3,558,872
- Sick leave benefits to be liquidated after one year 114,372
- Accrued unfunded other post-employment benefits liability 111,817
- **Total noncurrent liabilities** 12,027,794
- **Total liabilities** 15,615,291

**Deferred inflows of resources**
- Deferred gain on pension valuation 57,703
- **Total deferred inflows of resources** 57,703

**Net position (deficit):**
- Net investment in capital assets (1,017,787)
- Unrestricted (3,037,153)
- **Total net position (deficit)** $ (4,054,940)

*See accompanying notes.*
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Statement of Revenues, Expenses and Changes in Net Position  
(In thousands)  

Year Ended June 30, 2015  

Operating revenues $ 3,865,458  

Operating expenses:  
Operations:  
   Fuel 1,887,245  
   Purchased power 789,717  
   Other production 89,948  
   Transmission and distribution 235,660  
   Customer accounting and collection 158,186  
   Administrative and general 375,553  
   Maintenance 270,001  
   Depreciation 382,354  
   Total operating expenses 4,188,664  
Operating loss (323,146)  

Non-operating income and charges  
Interest income and other 44,263  
Interest charges:  
   Interest on bonds 422,330  
   Interest on notes payable and other long-term debt 55,416  
   Amortization of debt premium discount, issuance cost and refunding loss (1,979)  
   Allowance for funds used during construction (7,489)  
   Total interest charges, net 468,278  
   Impairment loss on GDB deposits (144,733)  
Loss before contribution in lieu of taxes and capital contributions (891,894)  

Contribution in lieu of taxes and other 273,460  
Loss before capital contributions (1,165,354)  

Capital contributions 21,464  
Changes in net position (1,143,950)  

Net position (deficit), beginning balance, as restated (2,910,950)  
Net position (deficit), ending balance $ (4,054,940)  

See accompanying notes.
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Statement of Cash Flows
(In thousands)

Year Ended June 30, 2015

Cash flows from operating activities
Cash received from customers $ 3,380,783
Cash paid to suppliers and employees (3,173,041)
Net cash flows provided by operating activities 207,742

Cash flows from noncapital financing activities
Proceeds from notes payable 11,566
Principal paid on notes payable (1,958)
Interest paid on notes payable (333)
Principal paid on fuel line of credit (156,930)
Proceeds from fuel line of credit 156,874
Interest paid on fuel line of credit (56,779)
Net cash flows used in noncapital financing activities (47,560)

Cash flows from capital and related financing activities
Construction expenditures (226,624)
Proceeds received from capital contributions 10,419
Power revenue bonds:
   Principal paid on revenue bonds maturities (204,305)
   Interest paid on revenue bonds (427,605)
Net cash flows used in capital and related financing activities (848,115)

Cash flows from investing activities
Purchases of investment securities (1,642,949)
Proceeds from sale and maturities of investment securities 1,930,251
Interest on investments 14,708
Transfer from restricted funds to general funds 5,000
Net cash flows provided by investing activities 307,020
Net decrease in cash and cash equivalents (380,913)
Cash and cash equivalents at beginning of year 781,451

Cash and cash equivalents at end of year $ 400,548

See accompanying notes. (continued)
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Statement of Cash Flows  
(In thousands)  

Year Ended June 30, 2015

Cash and cash equivalents  
Unrestricted $ 264,653  
Restricted:  
Cash and cash equivalents within construction and other special funds $ 135,895  
$ 400,548

Reconciliation of operating income to net cash provided by operating activities  
Operating income (323,146)  
Adjustments to reconcile operating income to net cash provided by operating activities:  
Depreciation 382,354  
Provision for uncollectible accounts and other 234,736  
Changes in assets and liabilities:  
Receivables (356,975)  
Fuel oil 130,538  
Materials and supplies 17,982  
Prepayments and other assets (3,465)  
Deferred outflows of resources (1,452,442)  
Other assets (11,707)  
Noncurrent liabilities, excluding revenue bonds and notes payable (7,504)  
Accounts payable and accrued liabilities (276,418)  
Net Pension Liability 1,814,744  
Deferred inflow of resources 57,703  
Customer’s deposits 1,342  
Total adjustments 530,888  
Net cash flows provided by operating activities $ 207,742

Supplemental cash flows information  
Noncash transactions:  
Capital contributions $ 12,464  
Change in fair value of derivative instruments $ (2,331)  
Changes in deferred loss resulting from debt refunding $ (11,594)

See accompanying notes.  
(concluded)
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Audited Financial Statements

June 30, 2015

1. Reporting Entity

Puerto Rico Electric Power Authority (the Authority) is a public corporation and governmental instrumentality of the Commonwealth of Puerto Rico (the Commonwealth) created on May 2, 1941, pursuant to Act No. 83, as amended, reenacted, and supplemented, of the Legislature of Puerto Rico (the Act) for the purpose of conserving, developing and utilizing the water, and power resources of Puerto Rico in order to promote the general welfare of the Commonwealth. Under the entity concept, the Authority is a component unit of the Commonwealth. The Authority transmits and distributes, substantially, all of the electric power consumed and produces a majority of the electricity generated in Puerto Rico.

The Authority has broad powers including, among others, to issue bonds for any of its corporate purposes subject to the limitations set forth in a Trust Agreement dated as of January 1, 1974, as amended (the 1974 Agreement). The Authority is required, under the terms of the 1974 Agreement and the Act, to determine and collect reasonable rates for electric service in order to produce revenues sufficient to cover all operating and financial obligations, as defined.

On August 18, 2003, the Commonwealth approved Act No. 189, which authorizes the Authority to create, acquire and maintain corporations, partnerships or subsidiary corporations, for profit or nonprofit entities.

On May 27, 2014, the Commonwealth approved Act No. 57, which authorizes the Puerto Rico Energy Commission to approve electric rates proposed by the Authority among other matters.

Basis of Presentation – Blended Component Units

The financial statements of the Authority as of the fiscal year ended June 30, 2015, include the financial position and operations of the Puerto Rico Irrigation Systems (Irrigation Systems) and PREPA Holdings, LLC (PREPA Holdings). The Irrigation Systems operate pursuant to the provisions of the Act, and Acts Nos. 83 and 84, approved on June 20, 1955, regarding the Puerto Rico Irrigation Service, South Coast, and Isabela Irrigation Service, respectively, and the Lajas Valley Public Irrigation Law, approved on June 10, 1953, as amended. PREPA Holdings, a wholly owned subsidiary of the Authority, was created for the sole purpose of acting as a holding company and has no current operations. PREPA Holdings is the direct parent of the following entities: PREPA Networks, LLC (PREPA.Net), Inter American Energy Sources, LLC, and Consolidated Telecom of Puerto Rico, LLC.
The Irrigations Systems and PREPA Holdings conform to the requirements of Governmental Accounting Standards Board (GASB) No. 61, *The Financial Reporting Entity: Omnibus amendment of GASB Statements No. 14 and No. 34, and No. 39, Determining Whether Certain Organizations are Component Units*, on its standalone financial statements. GASB No. 39 establishes standards for defining and reporting on the financial reporting entity. It also establishes standards for reporting participation in joint ventures. It applies to financial reporting by primary governments, and other standalone governments; and it applies to the separately issued financial statements of governmental component units. In addition, this Statement should be applied to governmental and nongovernmental component units when they are included in a governmental financial reporting entity.

Condensed financial information as of June 30, 2015 for the Irrigation Systems is as follows:

<table>
<thead>
<tr>
<th></th>
<th>(In thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Statements of net position:</strong></td>
<td></td>
</tr>
<tr>
<td>Assets:</td>
<td></td>
</tr>
<tr>
<td>Receivables, net</td>
<td>$ 9,176</td>
</tr>
<tr>
<td>Prepayments and other assets</td>
<td>240</td>
</tr>
<tr>
<td>Capital assets, net of depreciation</td>
<td>20,337</td>
</tr>
<tr>
<td>Total assets</td>
<td>$ 29,753</td>
</tr>
<tr>
<td>Liabilities:</td>
<td></td>
</tr>
<tr>
<td>Accounts payable</td>
<td>$ 1,066</td>
</tr>
<tr>
<td><strong>Statements of revenues, expenses and changes in net position:</strong></td>
<td></td>
</tr>
<tr>
<td>Operating revenues</td>
<td>$ 5,987</td>
</tr>
<tr>
<td>Operating expenses</td>
<td>(3,092)</td>
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<tr>
<td>Change in net position</td>
<td>2,895</td>
</tr>
<tr>
<td>Net position, beginning balance</td>
<td>25,792</td>
</tr>
<tr>
<td>Net position, ending balance</td>
<td>$ 28,687</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  
June 30, 2015

Pursuant to the Act, the Authority is authorized to create subsidiaries in order to, among other things, delegate or transfer any of its rights, powers, functions or duties. The Authority currently has four principal subsidiaries organized in a holding company structure.

PREPA.Net, a subsidiary of the Authority, was formed for the purpose of merging two local not-for-profit entities – PREPA Networks, Corp, and PREPA.Net International Wholesale Transport, Inc.

PREPA.Net markets the excess communication capacity of the Authority’s fiber optic cable system. PREPA.Net currently offers next generation telecommunications services to carriers, internet service providers, and large commercial enterprises. These services include data transmission via Synchronous Optical Network (SONET), metro and long-haul Ethernet transport services, wireless last mile, and internet protocol services optimized for voice over internet protocol. PREPA.Net also offers international fiber optic cable capacity and satellite teleport facilities through the submarine fiber optic cable capacity acquired in 2008.

InterAmerican Energy Sources, LLC was created on May 25, 2007, as a Delaware limited liability company, for the purpose of investing, developing, financing, constructing and operating renewable energy projects and other infrastructure related to the optimization of the Authority’s electric infrastructure. InterAmerican Energy Sources, LLC is currently not operating.

Consolidated Telecom of Puerto Rico, LLC was created on October 27, 2009, as a Delaware limited liability company, for the purpose of developing, financing, constructing and operating a telecommunications business within or outside of the Commonwealth, directly or indirectly, in relation to the operations of the Authority.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  

June 30, 2015  

Condensed financial information for PREPA Holdings, LLC as of June 30, 2015 is as follows:

<table>
<thead>
<tr>
<th>Statement of net position:</th>
<th>(In thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets:</td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$ 8,685</td>
</tr>
<tr>
<td>Certificate of deposits</td>
<td>1,642</td>
</tr>
<tr>
<td>Receivables, net</td>
<td>3,031</td>
</tr>
<tr>
<td>Prepayments and other assets</td>
<td>135</td>
</tr>
<tr>
<td>Capital assets, net of depreciation</td>
<td>48,421</td>
</tr>
<tr>
<td>Other receivables</td>
<td>9,518</td>
</tr>
<tr>
<td>Total assets</td>
<td>$ 71,432</td>
</tr>
</tbody>
</table>

| Liabilities:              |                |
| Accounts payable          | $ 21,731       |
| Notes payable             | 22,484         |
| Total liabilities         | $ 44,215       |

| Statements of revenues, expenses and changes in net position: |
| Operating revenues       | $ 18,958       |
| Operating expenses       | (11,830)       |
| Interest charge          | (333)          |
|                         | 6,795          |

Net position, beginning balance  
$ 20,422

Net position, ending balance  
$ 27,217
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Audited Financial Statements

June 30, 2015

Statement of cash flows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (In thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash flows from operating activities</td>
<td>$10,266</td>
</tr>
<tr>
<td>Cash flows from noncapital financing activities</td>
<td>$(1,070)</td>
</tr>
<tr>
<td>Cash flows from capital and related financing activities</td>
<td>$(8,808)</td>
</tr>
<tr>
<td>Cash flows from investing activities</td>
<td>-</td>
</tr>
<tr>
<td>Net increase in cash</td>
<td>$388</td>
</tr>
<tr>
<td>Cash at beginning of year</td>
<td>$8,297</td>
</tr>
<tr>
<td>Cash at end of year</td>
<td>$8,685</td>
</tr>
</tbody>
</table>

2. Summary of Significant Accounting Policies

The following is a summary of the most significant accounting policies followed by the Authority in preparing its financial statements:

Basis of Accounting

The accounting and reporting policies of the Authority conform to the accounting rules prescribed by the Governmental Accounting Standards Board (GASB). As such, it functions as an enterprise fund. The Authority maintains its accounting records on the accrual basis of accounting in conformity of US generally accepted accounting principles. Although the Authority is not subject to all Federal Energy Regulatory Commission (FERC) regulations, the Authority has adopted the uniform system of accounts prescribed by FERC.

The Authority accounts for its operations and financings in a manner similar to private business enterprises; the intent is that costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. Such accounts and these financial statements have been prepared on the basis that the Authority will continue as a going concern. Additional disclosures within the Notes to these financial statements, should be read in connection with consideration of the future ability of the Authority to continue as such.

Cash and Cash Equivalents

The Authority considers all highly liquid debt instruments with maturities of three months or less when purchased to be cash equivalents. Cash and cash equivalents included in the restricted funds are considered cash equivalents for purposes of the statement of cash flows.
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Audited Financial Statements
June 30, 2015

Receivables

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions, among other factors. The Authority establishes a general or specific reserve for each group of customers (i.e., residential, commercial, industrial, and governmental). The Authority has significant amounts receivable from the Commonwealth and its instrumentalities. There is significant uncertainty in regard to the collection of such receivables due to the financial challenges these entities are facing. The Authority has considered this in its estimate of the specific governmental reserve for uncollectible accounts. Because of uncertainties inherent in the estimation process, management’s estimate of credit losses inherent in the existing accounts receivable and related allowance may change in the future.

Materials, Supplies and Fuel Oil

Materials, supplies and fuel oil inventories are carried at average cost and are stated at the lower of cost or market.

Investments

The Authority follows the provisions of GASB Statement No. 31, Accounting and Financial Reporting for Certain Investments and for External Investment Pools, which require the reporting of investments at fair value in the statement of net position and recording changes in fair value in the statements of revenues, expenses and changes in net position. The fair value is based on quoted market prices and recognized pricing services for certain fixed income securities.

The funds under the 1974 Agreement may be invested in:

- Government obligations, which are direct obligations of, or obligations whose principal and interest is guaranteed by the U.S. Government, or obligations of certain of its agencies or instrumentalities.

- Investment obligations of any of the states or territories of the United States or political subdivisions thereof (other than obligations rated lower than the three highest grades by a nationally recognized rating agency) and repurchase agreements with commercial banks fully secured by U.S. Government obligations.
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• Time deposits with Government Development Bank for Puerto Rico (GDB) or the Authority’s Trustee under the 1974 Agreement or any bank or trust company member of the Federal Deposit Insurance Corporation having a combined capital and surplus of not less than $100 million.

In April 1999, the 1974 Agreement was amended to provide that permitted investments of moneys to the credit of the self-insurance Fund be expanded (subject to the Authority’s adoption of an investment policy with the consent of GDB) to coincide with the investments permitted for the pension fund for employees of the Commonwealth of Puerto Rico and its Instrumentalities.

Such investments include various debt instruments, such as mortgage loans and leases, common and preferred stock, real property and various other financial instruments.

Capital Assets

Utility plant is carried at cost, which includes labor, materials, overhead, and an allowance for the cost of funds used during construction (AFUDC). AFUDC represents the cost of borrowed funds used to finance construction work in progress. AFUDC is capitalized as an additional cost of property and as a reduction of interest expense. Capitalized interest expense is reduced by interest income earned on related investments acquired with proceeds of tax-exempt borrowings. Such costs are recovered from customers as a cost of service through depreciation charges in future periods. Capitalized interest during the year ended June 30, 2015 amounted to $7.5 million. This amount is net of interest income earned on investments amounting to $2.2 million.

Capital expenditures of $1,200 or more are capitalized at cost at the date of acquisition. Maintenance, repairs, and the cost of renewals of minor items of property units are charged to operating expenses. Replacements of major items of property are charged to the plant accounts. The cost of retired property, together with removal cost less salvage, is charged to accumulated depreciation with no gain or loss recognized.

The Authority follows the provisions of GASB Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries, as amended. This statement establishes guidance for accounting and reporting for the impairment of capital assets and for insurance recoveries.
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Depreciation  

Depreciation is computed on the straight-line method at rates considered adequate to allocate the cost of the various classes of property over their estimated service lives. The annual composite rate of depreciation, determined by the Authority’s consulting engineers, was approximately 3.58% for 2015.

Unamortized Debt Issuance Cost and Debt Related Deferrals  

Debt issuance costs are recorded as expenses during the year they are incurred. Premium and discounts incurred in the issuance of bonds are deferred and amortized using the straight-line method, which approximates the interest method, over the term of the related debt.

For refunding debt, the excess of reacquisition cost over the carrying value of the corresponding long-term debt is deferred and amortized to operating expenses using the straight-line method over the remaining life of the original debt or the life of the new debt, whichever is shorter.

Bonds payable are reported net of applicable bond premium or discount. The unamortized deferred losses from debt refundings are reported as deferred outflows of resources in the accompanying statement of net position.

Pensions  

For purposes of measuring the net pension liability and deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Authority’s Pension Plan administered by PREPA’s Employee Retirement System (the System) and additions to/deductions from the Plans’ fiduciary net position have been determined on the same basis as they are reported by the System. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Accounting for Compensated Absences  

Employees earn annual vacation leave at the rate of 30 days per year up to a maximum permissible accumulation of 60 days for union employees and management personnel.
Employees accumulate sick leave at the rate of 19 days per year. Sick leave is only payable if the regular employee resigns and has more than 10 years of employment, or retires and takes a pension. Maximum permissible accumulation for sick leave is 90 days for all employee and the excess shall be lost if an employee does not use such excess from January to June of the next year.

The Authority records as a liability and as an expense the vested accumulated vacation and sick leave as benefits accrue to employees. The cost of vacation and sick leave expected to be paid in the next twelve months is classified as current and accrued liabilities while amounts expected to be paid after twelve months are classified as noncurrent liabilities.

Revenue Recognition, Fuel Costs and Purchased Power

Clients are billed monthly. Revenues are recorded based on services rendered during each accounting period net of discounts and allowances, including an estimate for unbilled services. Revenues include amounts resulting from a fuel and purchased power cost recovery clause (Fuel Adjustment Clause), which is designed to permit full recovery through customer billings of fuel costs and purchased power. Fuel costs and purchased power are reflected in operating expenses as the fuel and purchased power are consumed.

Contributions in Lieu of Taxes and Governmental Subsidies

The Act exempts the Authority from all taxes that otherwise would be levied on its properties and revenues by the Commonwealth and its Municipalities, except to the extent net revenues, as defined, are available, wherein the Authority is required under the Act to make a contribution in lieu of taxes to the Commonwealth and the Municipalities of 11% of gross electric sales as follows:

Municipalities

The Authority is required under the Act to make a contribution in lieu of taxes to municipalities of the greater of:

a) Twenty percent of the Authority's Adjusted Net Revenues (Net Revenues, as defined in the 1974 Agreement, less the cost of the Commonwealth rate subsidies);
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b) The cost collectively of the actual electric power consumption of the municipalities; or
c) The prior five-year moving average of the contributions in lieu of taxes paid to the municipalities collectively.

If the Authority does not have sufficient funds available in any year to pay the contribution in lieu of taxes, the difference is accrued and carried forward for a maximum of three years. The contribution in lieu of taxes to Municipalities can be used to offset accounts receivable balance owed by the Municipalities to the Authority as permitted by law.

Commonwealth of Puerto Rico

To the extent net revenues are available, the Authority is also required under the Act to set aside the remainder of contribution in lieu of taxes for the purpose of (i) financing capital improvements, (ii) offsetting other subsidies (other than cost of fuel adjustments to certain residential clients) of the Commonwealth, and (iii) any other lawful corporate purpose. Amounts assigned to (ii) above, are classified as a contribution in lieu of taxes in the accompanying statement of revenues, expenses and changes in net position and reduce the related accounts receivable in the statement of net position.

Capital Contributions

The Authority records contributed capital as income in the year earned. The Authority receives contributed capital in the form of cash and property from residential projects developed by third parties during recent years and local and federal agencies. During the year ended June 30, 2015, the Authority received cash and non-cash contributed capital in the amount of $8,940 million and $12,464 million, respectively.

Risk Management

The Authority purchases commercial insurance covering casualty, theft, tort claims, natural disaster and other claims covering all risk property (excluding transmission and distribution lines), boiler and machinery, boiler, machinery and public liability. In addition, the Authority has a self-insured fund to pay the cost of repairing, replacing or reconstructing any property damaged or destroyed from, or extraordinary expenses incurred as a result of a cause, which is not covered by insurance required under 1974 agreement.
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Estimates  

The preparation of the basic financial statements in conformity with U.S. generally accepted 
accounting principles (GAAP) requires management to make estimates and assumptions that 
affect the reported amounts of assets (including related allowances for uncollectible accounts) 
and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial 
statements and the reported amounts of revenue and expenses during the reporting period. Actual 
results could differ from those estimates.  

Interest-Rate Swap Agreements  

The Authority follows the provisions of GASB Statement No. 53, Accounting and 
Financial Reporting for Derivative Instruments, as amended. This statement establishes guidance 
for the recognition, measurement, and disclosure of information regarding derivative instruments. 

The interest-rate swaps are used in the area of debt management to take advantage of favorable 
market interest rates and to limit interest rate risk associated with variable rate debt exposure. 

Under the interest-rate swap programs, the Authority pays fixed and variable rates of interest 
based on various indices for the term of the variable interest rate Power Revenue Bonds and 
receives a variable rate of interest, which is also based on various indices. These indices are 
affected by changes in the market. The net amount received or paid under the swap agreements is 
recorded as an adjustment to interest expense in the statement of revenues, expenses and changes 
in net position. The interest rate swaps are reported at fair value in the Statement of Net Position. 
The changes in fair value for effective hedges are recorded as deferred inflows or outflows of 
resources in the Statement of Net Position. The changes in fair value for ineffective hedges are 
reported in investment income.  

Restricted Assets  

Funds set aside for construction, debt service payments or other specific purposes are classified 
as restricted assets since their use is limited for these purposes by the applicable agreements. 

When both restricted and unrestricted resources are available for a specific use, it is the 
Authority’s policy to use restricted resources first, then unrestricted resources as they are needed.
Claims and Judgments

The estimated amount of the liability for claims and judgments is recorded on the accompanying statement of net position based on the Authority’s evaluation of the probability of an unfavorable outcome in the litigation of such claims and judgments. The Authority consults with legal counsel upon determining whether an unfavorable outcome is expected. Because of uncertainties inherent in the estimation process, management’s estimate of the liability for claims and judgments may change in the future.

Implementation of new accounting standards

Effective July 1, 2014, the Authority adopted GASB Statement No. 68 “Accounting and Financial Reporting for Pensions”, (Statement No. 68) and GASB Statement No. 71 “Pension Transition for Contributions Made Subsequent to the Measurement Date” (Statement No. 71), which amend the requirements of GASB Statement No. 27 “Accounting for Pensions by State and Local Governmental Employers” as they relate to governmental employers that account for pensions provided through trusts or equivalent arrangements.

This Statement replaces the requirements of GASB Statement No. 27, Accounting for Pensions by State and Local Governmental Employers, as well as the requirements of GASB Statement No. 50, "Pension Disclosures", as they relate to pensions that are provided through pension plans within the scope of the Statement. The requirements of GASB Statement No. 68 apply to the financial statements of all state and local governmental employers whose employees (or volunteers that provide services to state and local governments) are provided with pensions through pension plans that are administered through trusts or equivalent arrangements as described above, and to the financial statements of state and local governmental nonemployer contributing entities that have a legal obligation to make contributions directly to such pension plans. This Statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, and deferred inflows of resources, and expense/expenditures related to pensions. Note disclosure and Required Supplementary Information requirements about pensions also are addressed. For defined benefit pensions, this Statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service.

The major fundamental change is switching from the existing “funding-based” accounting model, where the Annual Required Contribution (ARC) was compared to the actual payments made and that difference determined the Net Pension Obligation (or Asset); to an “accrual basis”
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model similar to current Financial Accounting Standards Board (“FASB”) standards, where the Total Pension Liability (Actuarially determined) is compared to the Plan’s Fiduciary Net Position (predominantly assets) and the difference represents the Net Pension Liability. The information to adopt this Statement predominantly was based on the new actuarial report prepared under the new GASB Statement No. 67, "Financial Reporting for Pension Plans" - an Amendment of GASB Statement No. 25).

GASB Statement No. 71 amends GASB Statement No. 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability.

The application of Statements No. 68 and Statement No. 71 establishes standards for measuring and recognizing liabilities, deferred outflows and inflows of resources and expenses related to the government sponsored pension plan.

Net pension liability:

- The Net pension liability as defined by Statement No. 68 is the difference between the actuarial present value of projected pension benefit payments attributable to employees’ past service and the Plan’s fiduciary net position. As of June 30, 2015, the net pension liability was $3,558.9 million. Previous to this guidance, a liability was recognized only to the extent that the actuarially calculated contributions were more than the contributions made to the plan.

Deferred outflows of resources and Deferred inflows of resources:

- In addition to assets, the Statement of Net Position reports a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents an increase in net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. Similarly, the Authority reports deferred inflows of resources in the Statement of Net Position in a separate section following Liabilities. This separate financial statement element, deferred inflows of resources, represents a reduction of net position and resources that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. As of June 30, 2015, there were $57.7 million in deferred inflows of resources related to pensions benefits.
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- Unrealized pension contributions made between the net pension liability measurement date and the employer’s fiscal year end are recognized as deferred outflows of resources to be included as an increase to the Plan fiduciary net position in the subsequent fiscal year. There are also deferred outflows of resources related to differences between expected and actual experience, and changes of assumptions. As of June 30, 2015, there were deferred outflow of resources related to pensions of $1,552.5 million.

Effects of implementing Statement No. 68 and Statement No. 71 were applied to the Statement of Net Position as of the implementation date of July 1, 2014. Additional information on the Authority’s implementation of the Statement No. 68 and Statement No. 71 applied to the Statement of Net Position can be found in Note 18 to the financial statements.

3. Cash and Cash Equivalents

The 1974 Agreement established the General Fund, the Revenue Fund, and certain other funds (see Note 5).

All revenues (other than income from investments and construction funds obtained from financing) are deposited in these funds. The moneys held in these funds are presented as unrestricted cash and cash equivalents in the statement of net position.

At June 30, 2015, the carrying amount and bank balance of cash deposits held by the Authority and restricted cash deposits held by the Trustee under the 1974 Agreement is as follows (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Carrying Amount</th>
<th>Bank Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unrestricted</td>
<td>$ 264,653</td>
<td>$ 263,913</td>
</tr>
<tr>
<td>Restricted:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Held by the Authority</td>
<td>$ 135,895</td>
<td>$ 136,076</td>
</tr>
<tr>
<td></td>
<td>$ 400,548</td>
<td>$ 399,989</td>
</tr>
</tbody>
</table>
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Impairment Loss of Deposits with the Government Development Bank for Puerto Rico (GDB)  

On April 6, 2016, the Puerto Rico Emergency Moratorium and Rehabilitation Act (Act No. 21) was approved. Act No. 21 allows the Governor to declare a moratorium on debt service payments and to stay related creditor remedies for temporary period for the Commonwealth, GDB, Economic Development Bank for Puerto Rico and certain government instrumentalities, including the Authority.  

On April 8, 2016, the Governor of Puerto Rico signed executive order, EO-2016-010, declaring GDB to be in a state of emergency pursuant to Act No. 21, implemented a regulatory framework governing GDB’s operations and liquidity, including establishing a procedure with respect to governmental withdrawals, payments and transfer requests in respect of funds held on deposit at GDB, its operations and liquidity, including establishing a procedure with respect to funds held on deposit at GDB and loan disbursements by GDB. These procedures resulted in restrictions on the ability of the Authority to withdraw any funds held on deposit at GDB.  

GDB faces significant risks and uncertainties, and it currently does not have sufficient liquid financial resources to meet its obligations as they come due, as further described below. Pursuant to recently enacted legislation, the Governor of the Commonwealth has ordered the suspension of withdrawals and transfers of deposits from GDB, and imposed a moratorium on debt obligations of GDB, among other measures.  

As a result, management concluded that the information available after June 30, 2015 but prior to the issuance of the Authority’s financial statements for the year ended June 30, 2015, indicates that it is probable that an impairment loss on the Authority’s cash deposits held with GDB exists.  

An impairment loss on deposits held with GDB was, therefore, recorded in the Authority’s financial statements for the year ended June 30, 2015 as follows (expressed in thousands):  

<table>
<thead>
<tr>
<th>Deposits Held with GDB as of June 30, 2015</th>
<th>Beginning Book Balance</th>
<th>Impairment Loss</th>
<th>Ending Book Balance</th>
<th>Bank Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash equivalents</td>
<td>$ 131,055</td>
<td>$ (118,495)</td>
<td>$ 12,560</td>
<td>$ 131,055</td>
</tr>
<tr>
<td>Construction and other funds</td>
<td>$ 152,828</td>
<td>$ (26,238)</td>
<td>$ 126,590</td>
<td>$ 152,828</td>
</tr>
<tr>
<td>Restricted Assets</td>
<td>$ 23,723</td>
<td></td>
<td>$ 23,723</td>
<td>$ 23,723</td>
</tr>
<tr>
<td>Total</td>
<td>$ 307,606</td>
<td>$ (144,733)</td>
<td>$ 162,873</td>
<td>$ 307,606</td>
</tr>
</tbody>
</table>
Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a bank failure, the bank’s deposits may not be returned. The Commonwealth requires that public funds deposited in commercial banks in Puerto Rico must be fully collateralized. Deposits maintained in GDB or the Economic Development Bank (EDB) are exempt from the collateral requirements established by the Commonwealth and thus represent custodial credit risk because in the event of GDB’s or EDB’s failure the Authority may not be able to recover the deposits. The Authority’s policy is to deposit funds with either institution which provides insurance or securities as collateral. Such collateral is held by the Department of the Treasury of the Commonwealth.

All moneys deposited with the Trustee or any other Depository under and as defined in the 1974 Agreement in excess of the amount guaranteed by the Federal Deposit Insurance Corporation or other federal agency are continuously secured by lodging with a bank or trust company approved by the Authority and by the Trustee as custodian, or, if then permitted by law, by setting aside under control of the trust department of the bank holding such deposit, as collateral security, Government Obligations (as defined in the 1974 Agreement) or other marketable securities.

4. Accounts Receivable

At June 30, 2015, receivables consist of (in thousands):

Current:
  Electric and related services:
    Government agencies and municipalities       $ 1,565,000
    Residential, industrial and commercial        852,298
    Recoveries under fuel adjustment clause under billed 5,312
    Unbilled services                             170,830
    Miscellaneous accounts and others             12,922
  Allowance for uncollectible accounts          (593,388)
  Receivable from insurance companies and other 15,000
  Accrued interest on investments                2,643
  $ 2,030,617
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Noncurrent:  
Electric and related services:  
Government agencies and municipalities $142,107  
Allowance for uncollectible accounts - noncurrent (67,460)  
$74,647  

The Authority has other subsidies and reimbursable costs receivable from the Commonwealth, which are reduced by means of charges (accounted for as a contribution in lieu of taxes and to the extent net revenues, as defined, are available) against a portion of the contribution in lieu of taxes, after the contribution in lieu of taxes to municipalities, it is required to set aside under the Act. The Authority has the right to offset amounts receivable from municipalities amounting to $1,428.1 million as of June 30, 2015, with contribution in lieu of taxes payable to such municipalities. The portion of accounts receivable and other governmental receivables not expected to be collected during the next fiscal year are reflected in the accompanying statement of net position as other noncurrent receivables. Further, the Authority has recorded an allowance for uncollectible accounts estimated at $83.8 million for 2015, in consideration of the financial difficulty being experienced by the Commonwealth and related entities and the risk receivables (both current and long term) from such entities are uncollectible.  

5. Restricted Assets  

At June 30, 2015, certain investments and cash deposits of the Authority were restricted to comply with long-term principal and interest debt service requirements (sinking funds) as well as for self-insurance. These restricted assets are held by the Trustee under the 1974 Agreement (see Note 3) in the following funds:  

1974 Reserve Account — Reserve for payment of principal of and interest on Power Revenue Bonds in the event moneys in Bond Service Account or Redemption Account are insufficient for such purpose.  

1974 self-insurance Fund — Fund to pay the cost of repairing, replacing or reconstructing any property damaged or destroyed from, or extraordinary expenses incurred as a result of a cause, which is not covered by insurance required under the 1974 Agreement. The 1974 self-insurance Fund also serves as an additional reserve for the payment of the principal of and interest on the Power Revenue Bonds, and meeting the amortization requirements to the extent that moneys in the Bond Service Account, the Redemption Account and the 1974 Reserve Account are insufficient for such purpose. The Authority did not make any deposits into the 1974 Self Insurance Fund during the fiscal year.
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Bond Service Account and Redemption Account (1974 Sinking Fund) — Current year requirements for principal of and interest on Power Revenue Bonds. The Authority did not make required deposits into 1974 Sinking Fund Principal and Interest during current fiscal year.

At June 30, 2015, cash, cash equivalents and investments held by the Trustee consist of (in thousands):

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1974 Sinking Fund – Interest and Capitalized Interest</td>
<td>$53,842</td>
</tr>
<tr>
<td>1974 Reserve Account</td>
<td>236,787</td>
</tr>
<tr>
<td>1974 Self-Insurance Fund</td>
<td>100,152</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>390,781</strong></td>
</tr>
</tbody>
</table>

Investments held by Trustee under the 1974 Agreement are invested exclusively in securities of the U.S. Government and its agencies.

The Authority also has cash and investment securities held by the trust department of a commercial bank restricted for the following purposes:

1974 Construction Fund — Special fund created by the 1974 Agreement. The proceeds of any Power Revenue Bonds issued for the purpose of paying the cost of acquiring or constructing improvements, together with the money received from any other source for such purpose, except proceeds which are (i) applied to the repayment of advances, (ii) deposited in the 1974 Reserve Account, (iii) deposited in the Bond Service Account as capitalized interest or (iv) used for the payment of financing expenses, shall be deposited in the 1974 Construction Fund and held by the Authority in trust. During fiscal year 2015, the Authority did not deposit any money into the 1974 Construction Fund.

Reserve Maintenance Fund — Fund to pay the cost of unusual or extraordinary maintenance or repairs, not recurring annually, and renewals and replacements, including major items of equipment. The Reserve Maintenance Fund also serves as an additional reserve for the payment of principal and interest on the Power Revenue Bonds and meeting the amortization requirements to the extent that moneys in the 1974 Sinking Fund, including money in the 1974 Reserve Account, are insufficient for such purpose. The Authority did not make any deposits into the 1974 Reserve Maintenance Fund during fiscal year 2015.
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At June 30, 2015, the 1974 Construction Fund, Reserve Maintenance Fund and other restricted funds consist of (in thousands):

<table>
<thead>
<tr>
<th></th>
<th>Cash and Cash Equivalents</th>
<th>Investments</th>
</tr>
</thead>
<tbody>
<tr>
<td>1974 Construction Fund</td>
<td>$ 133,966</td>
<td>$ 1,106</td>
</tr>
<tr>
<td>Reserve Maintenance Fund</td>
<td>-</td>
<td>16,040</td>
</tr>
<tr>
<td>Other Restricted Funds</td>
<td>1,929</td>
<td>-</td>
</tr>
<tr>
<td>PREPA Client Fund</td>
<td>-</td>
<td>3,180</td>
</tr>
<tr>
<td></td>
<td><strong>$ 135,895</strong></td>
<td><strong>$ 20,326</strong></td>
</tr>
</tbody>
</table>

Following is the composition of the investments in the 1974 Construction Fund and other special funds (in thousands):

```
<table>
<thead>
<tr>
<th>Investment</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Government obligations</td>
<td>$ 1,106</td>
</tr>
<tr>
<td>Certificate of deposit</td>
<td>19,220</td>
</tr>
<tr>
<td></td>
<td><strong>$ 20,326</strong></td>
</tr>
</tbody>
</table>
```

Investments

The following table provides a summary of the Authority’s investments by type at June 30, 2015 (in thousands):

<table>
<thead>
<tr>
<th>1974 Reserve Maintenance Fund</th>
<th>Coupon Rate</th>
<th>Maturity Dates</th>
<th>Face Value</th>
<th>Fair Value</th>
<th>% of Total Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Certificate of Deposits</td>
<td>Various</td>
<td>9/30/15</td>
<td>$ 16,040</td>
<td>$ 16,040</td>
<td>100 %</td>
</tr>
<tr>
<td>Total Portfolio</td>
<td></td>
<td></td>
<td><strong>$ 16,040</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| 1974 Self Insurance Fund     |             |                |            |            |                      |
| Federal Home Loan Mortgage Corp. | 5.000 to 6.5% | 04/2020 to 11/2028 | $ 2,153 | $ 2,381 | 2.4 %                |
| Federal National Mortgage Association | 5.000 to 6.5% | 06/2022 to 07/2014 | 5,834 | 6,413 | 6.4 %                |
| Corporate Issues             | 3.45 to 4.65% | 05/2024 | 1,510 | 1,570 | 1.6 %                |
| U.S. Bank Money Market       | .02%         | Various | 57,935 | 57,931 | 57.8 %               |
| U.S. Treasury Note           | 2.00 to 6.25% | 11/2021 | 15,620 | 16,565 | 16.56 %              |
| U.S. Treasury Bonds          | 8.13%        | 08/2021 | 650 | 886 | 0.9 %                |
| Domestic Common Stocks       | Various      | Various | 10,523 | 14,406 | 14.4 %               |
| Total Portfolio              |             |                | **100,152** |            |                      |
Puerto Rico Electric Power Authority  
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<table>
<thead>
<tr>
<th>1974 Reserve Account</th>
<th>Coupon Rate</th>
<th>Maturity Dates</th>
<th>Face Value</th>
<th>Fair Value</th>
<th>% of Total Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Bank Money Market</td>
<td>0.2%</td>
<td>Various</td>
<td>$236,787</td>
<td>$236,787</td>
<td>99.5%</td>
</tr>
<tr>
<td>Total Portfolio</td>
<td></td>
<td></td>
<td>$236,787</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Sinking Fund - Capitalized Interest</th>
<th>Coupon Rate</th>
<th>Maturity Dates</th>
<th>Face Value</th>
<th>Fair Value</th>
<th>% of Total Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Bank Money Market</td>
<td>2.000%</td>
<td>Various</td>
<td>$25,022</td>
<td>$25,021</td>
<td>51.3%</td>
</tr>
<tr>
<td>Certificates of Deposit</td>
<td>1.900%</td>
<td>Various</td>
<td>$23,723</td>
<td>$23,723</td>
<td>48.7%</td>
</tr>
<tr>
<td>Total Portfolio</td>
<td></td>
<td></td>
<td>$48,744</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>1974 Sinking Fund</th>
<th>Coupon Rate</th>
<th>Maturity Dates</th>
<th>Face Value</th>
<th>Fair Value</th>
<th>% of Total Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Bank Money Market</td>
<td>0.2%</td>
<td>Various</td>
<td>$5,098</td>
<td>$5,098</td>
<td>100.0%</td>
</tr>
<tr>
<td>Total Portfolio</td>
<td></td>
<td></td>
<td>$5,098</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>1974 PREPA Client</th>
<th>Coupon Rate</th>
<th>Maturity Dates</th>
<th>Face Value</th>
<th>Fair Value</th>
<th>% of Total Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Certificates of Deposit</td>
<td></td>
<td></td>
<td>$3,180</td>
<td>$3,180</td>
<td>100.0%</td>
</tr>
<tr>
<td>Total Portfolio</td>
<td></td>
<td></td>
<td>$3,180</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>1974 Construction Fund</th>
<th>Other - Rural Electrification Administration (REA)</th>
<th>Coupon Rate</th>
<th>Maturity Dates</th>
<th>Face Value</th>
<th>Fair Value</th>
<th>% of Total Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>0.2%</td>
<td>Various</td>
<td>$1,106</td>
<td>$1,106</td>
<td>100.0%</td>
</tr>
<tr>
<td>Total Portfolio</td>
<td></td>
<td></td>
<td></td>
<td>$1,106</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Credit Risk**

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The 1974 Trust Agreement limits investments in:

- Government obligations, which are direct obligations of or obligations whose principal and interest is guaranteed by the U.S. Government, or obligations of certain of its agencies or instrumentalities.

- Investment obligations of any of the states or territories of the United States or political subdivisions thereof (other than obligations rated lower than the three highest grades by a nationally recognized rating agency) and repurchase agreements with commercial banks fully secured by U.S. Government Obligations.

- Certificates of deposits with GDB or the Authority’s Trustee under the 1974 Agreement or any bank or trust company member of the Federal Deposit Insurance Corporation having a combined capital and surplus of not less than $100 million.

- self-insurance fund and PREPA client fund are allowed to invest in corporate issues, with certain restrictions (40% of the total fixed income portfolio).
As of June 30, 2015, the Authority’s investments in Federal Home Loan Mortgage, Federal Home Loan Bank, Federal National Mortgage Association and Federal Farm Credit Bank and Freddie Mac were rated AA+ by Standard & Poor’s (S&P) and Aaa by Moody’s Investors Service.

Concentration Credit Risk

Concentration of credit risk is the risk of loss attributable to the magnitude of investment in a single issuer by five percent or more of total investment. The Authority’s investment policy does not contain a limitation to invest in the securities of single issuer. The Authority maintains deposit with high rated financial institutions and with the GDB. Deposits with GDB are exempt from the collateralization requirement and represent a custodial credit risk. As of June 30, 2015, the Authority held uncollateralized deposits in GDB of $23.7 million.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. Information about the sensitivity of the fair values of the Authority’s investment to market interest fluctuations is provided by the following tables that show the distribution of the investments by maturity as of June 30, 2015 (in thousands):

<table>
<thead>
<tr>
<th>Investment Type</th>
<th>Fair Value</th>
<th>Investment Maturities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Less than 1 year</td>
</tr>
<tr>
<td>Federal Home Loan Mortgage Corp.</td>
<td>$2,380</td>
<td>$ -</td>
</tr>
<tr>
<td>Federal National Mortgage Association</td>
<td>6,413</td>
<td>-</td>
</tr>
<tr>
<td>Certificates of Deposit</td>
<td>42,943</td>
<td>42,943</td>
</tr>
<tr>
<td>Other-REA Investment</td>
<td>1,106</td>
<td>-</td>
</tr>
<tr>
<td>U.S. Treasury Note</td>
<td>16,563</td>
<td>-</td>
</tr>
<tr>
<td>U.S. Treasury Bonds</td>
<td>886</td>
<td>-</td>
</tr>
<tr>
<td>U.S. Bank Money Market</td>
<td>324,840</td>
<td>324,840</td>
</tr>
<tr>
<td>Domestic Common Stocks</td>
<td>14,406</td>
<td>-</td>
</tr>
<tr>
<td>Corporate issues</td>
<td>1,570</td>
<td>-</td>
</tr>
<tr>
<td>Total Investments</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
6. Capital Assets

As of June 30, 2015, capital assets consist of:

<table>
<thead>
<tr>
<th></th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Distribution</td>
<td>$ 4,159,187</td>
</tr>
<tr>
<td>Transmission</td>
<td>2,367,224</td>
</tr>
<tr>
<td>Production</td>
<td>2,950,802</td>
</tr>
<tr>
<td>Other production</td>
<td>1,544,248</td>
</tr>
<tr>
<td>Hydroelectric</td>
<td>142,268</td>
</tr>
<tr>
<td>General</td>
<td>1,572,851</td>
</tr>
<tr>
<td>Irrigation systems</td>
<td>35,277</td>
</tr>
<tr>
<td>Fiber Network</td>
<td>43,888</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>12,815,745</strong></td>
</tr>
</tbody>
</table>

Less accumulated depreciation

<table>
<thead>
<tr>
<th></th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(6,787,733)</td>
</tr>
<tr>
<td>Construction in progress</td>
<td>6,028,012</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>671,333</strong></td>
</tr>
<tr>
<td></td>
<td><strong>6,699,345</strong></td>
</tr>
</tbody>
</table>

Capital asset activity for the fiscal years ended June 30, 2015 was as follows (in thousands):

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Plant in service</td>
<td>$ 12,281,158</td>
<td>$ -</td>
<td>$ (14,780)</td>
<td>$ 549,367</td>
<td>$ 12,815,745</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Construction work in progress</td>
<td>988,524</td>
<td>232,176</td>
<td>-</td>
<td>(549,367)</td>
<td>671,333</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total capital assets</td>
<td>13,269,682</td>
<td>232,176</td>
<td>(14,780)</td>
<td>-</td>
<td>13,487,078</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Less:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Accumulated depreciation</td>
<td>(6,422,225)</td>
<td>(382,354)</td>
<td>16,846</td>
<td>-</td>
<td>(6,787,733)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total capital assets, net</td>
<td>$ 6,847,457</td>
<td>$(150,178)</td>
<td>$ 2,066</td>
<td>-</td>
<td>$ 6,699,345</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Construction work in progress at June 30, 2015 consists principally of expansions and upgrades to the electric generation, distribution and transmission systems.
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Audited Financial Statements

June 30, 2015

7. Defeasance of Debt

In prior years, the Authority has refunded in advance certain Power Revenue Bonds and other obligations by placing the proceeds of new debt in an irrevocable trust to provide for future debt service payments on such bonds. Accordingly, the trust accounts, assets, and liabilities for the defeased bonds are not included in the Authority’s financial statements. At June 30, 2015, $3.5 million of Power Revenue Bonds which remain outstanding were considered defeased.

8. Notes Payable

The following is a summary of notes payable as of June 30, 2015 (in thousands):

<table>
<thead>
<tr>
<th>Notes payable, unrestricted:</th>
<th>June 30, 2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maturity Date</td>
<td>Effective Interest Rate</td>
</tr>
<tr>
<td>Revolving line of credit of $253 million to finance working capital</td>
<td>Jan-15</td>
</tr>
<tr>
<td>Revolving line of credit of $500 million to finance working capital</td>
<td>Aug-14</td>
</tr>
<tr>
<td>Line of credit of $25 million to finance improvements to Isabela Irrigation System</td>
<td>June-18</td>
</tr>
<tr>
<td>Revolving line of credit of $100 million to fund swap’s collateral posting</td>
<td>Dec-14</td>
</tr>
<tr>
<td>P.R. (ULTRACOM)</td>
<td>Feb-23</td>
</tr>
<tr>
<td>PREPA Holdings (IT Solution)</td>
<td>May-17</td>
</tr>
<tr>
<td>Total notes payable</td>
<td></td>
</tr>
</tbody>
</table>

(V) - variable interest rate
(F) - fixed interest rate

On July 2, 2017 Puerto Rico Electric Power Authority ("PREPA") filed a petition in the United States District Court for the District of Puerto Rico for relief under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"). PREPA intends to propose a plan for the adjustment of its debts (although such intention should not preclude efforts to implement consensual debt restructurings if possible and practicable). [See Note 19 and 20]
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Audited Financial Statements

June 30, 2015

Short-term debt activity for the years ended June 30, 2015 was as follows:

(In thousands)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance at beginning of year</td>
<td>$733,908</td>
</tr>
<tr>
<td>Proceeds and transfers from long-term debt</td>
<td>156,874</td>
</tr>
<tr>
<td>Payment of short-term debt</td>
<td>(156,930)</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td>$733,852</td>
</tr>
</tbody>
</table>

9. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities at June 30, 2015 were as follows:

(In thousands)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts payable, accruals, and withholdings in process of payment</td>
<td>$504,099</td>
</tr>
<tr>
<td>Additional accruals and withholdings:</td>
<td></td>
</tr>
<tr>
<td>Injuries, damages and other</td>
<td>52,886</td>
</tr>
<tr>
<td>Accrued vacation and payroll benefits</td>
<td>60,482</td>
</tr>
<tr>
<td>Accrued sick leave and payroll benefits - exclusive of benefits</td>
<td></td>
</tr>
<tr>
<td>to be liquidated after one year of approximately $114.4 million in 2015</td>
<td>23,108</td>
</tr>
<tr>
<td>Accrued compensation</td>
<td>12,028</td>
</tr>
<tr>
<td>Accrued pension plan contribution and withholding from employees</td>
<td>25,478</td>
</tr>
<tr>
<td>Contribution in lieu of taxes</td>
<td>1,428,050</td>
</tr>
<tr>
<td>Other accrued liabilities</td>
<td>34,835</td>
</tr>
<tr>
<td></td>
<td>$2,140,966</td>
</tr>
</tbody>
</table>

10. Other Current Liabilities Payable from Restricted Assets

(In thousands)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contract retainage</td>
<td>$1,179</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>36,522</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$37,701</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to Audited Financial Statements
June 30, 2015

11. Long-term Debt

At June 30, 2015, long-term debt consists of:

(In thousands)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Power Revenue Bonds payable:</td>
<td></td>
</tr>
<tr>
<td>Publicly offered at various dates from 2002 to 2013, interest rates</td>
<td>$8,322,405</td>
</tr>
<tr>
<td>ranging from 2.5 to 7.25%, maturing to 2043</td>
<td></td>
</tr>
<tr>
<td>Plus, unamortized premium/discount, net</td>
<td>$126,521</td>
</tr>
<tr>
<td>Revenue bonds payable, net</td>
<td>8,448,926</td>
</tr>
<tr>
<td>Notes payable and bond anticipation notes</td>
<td>754,322</td>
</tr>
<tr>
<td></td>
<td>9,203,248</td>
</tr>
</tbody>
</table>

Less current portion of long-term debt:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Notes payable from unrestricted assets</td>
<td>733,852</td>
</tr>
<tr>
<td>Power revenue bonds</td>
<td>449,254</td>
</tr>
<tr>
<td>Total current: portion of long-term debt</td>
<td>1,183,106</td>
</tr>
<tr>
<td></td>
<td>$8,020,142</td>
</tr>
</tbody>
</table>

Long-term debt activity for the year ended June 30, 2015 was as follows:

(In thousands)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-term debt excluding current portion at beginning of year</td>
<td>$9,413,195</td>
</tr>
<tr>
<td>New issues:</td>
<td></td>
</tr>
<tr>
<td>Notes payable</td>
<td>168,440</td>
</tr>
<tr>
<td></td>
<td>9,581,635</td>
</tr>
<tr>
<td>Payments:</td>
<td></td>
</tr>
<tr>
<td>Power Revenue Bonds – July 1</td>
<td>(204,305)</td>
</tr>
<tr>
<td>Notes payable</td>
<td>(158,888)</td>
</tr>
<tr>
<td>Total payments</td>
<td>(363,193)</td>
</tr>
<tr>
<td>Amortization of debt discount</td>
<td>(15,194)</td>
</tr>
<tr>
<td>Balance at end of year</td>
<td></td>
</tr>
<tr>
<td></td>
<td>9,203,248</td>
</tr>
<tr>
<td>Current portion of notes payable</td>
<td>$733,852</td>
</tr>
<tr>
<td>Current portion of power revenue bonds</td>
<td>449,254</td>
</tr>
<tr>
<td>Total current portion of long-term debt</td>
<td>$1,183,106</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  
June 30, 2015  

Power Revenue Bonds Payable  

During fiscal year 2015, the Authority has not issued Power Revenue Bonds.  

The Authority has issued Power Revenue Bonds pursuant to the 1974 Agreement principally for the purpose of financing the cost of improvements, as such term is defined in the 1974 Agreement, and subject to the conditions and limitations set forth therein.  

In the 1974 Agreement, the Authority covenants to fix, charge, and collect rates so that revenues will be sufficient to pay current expenses and to provide the greater of (i) the required deposits or transfers to the Sinking Fund, the 1974 self-insurance Fund and the Reserve Maintenance Fund or (ii) 120% of the aggregate principal and interest requirements for the next fiscal year on account of all outstanding Power Revenue Bonds.  

According to the 1974 Agreement, gross revenues, exclusive of income on certain investments, less current expenses as defined in the 1974 Agreement should be pledged to repay Power Revenue Bonds principal and interest. As a result of the filing of Title III from PROMESA Act, the Authority is currently not in compliance with certain terms of its Trust Agreement.  

Title III of PROMESA establishes an in-court process for restructuring the debts off Puerto Rico and other United States territories that is modeled after the process under Chapter 9 of the U.S Bankruptcy Code. In order to be a debtor under Title III, the territory and/or its instrumentalities must: (i) have an Oversight Board established for it to be designated a “covered entity”; (ii) have the Oversight Board issue a restructuring certification under PROMESA section 206 (b); and (iii) “desire to effect a plan to adjust its debt.” The Oversight Board has sole authority to file a voluntary petition seeking protection under Title III of PROMESA. As of December 14, 2017, the Oversight Board has commenced Title III cases for the Commonwealth and the Authority.  

Swap Agreements  

To protect against the potential of rising interest rates, the Authority entered into quarterly separate pay-fixed and receive-variable interest-rate swap agreements at a cost anticipated to be less than what the Authority would have paid to issue fixed-rate debt. On June 30, 2015, the Authority had the following derivative instruments outstanding (in thousands):
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  

June 30, 2015  

<table>
<thead>
<tr>
<th>Item</th>
<th>Type</th>
<th>Objective</th>
<th>Effective Date</th>
<th>Maturity Date</th>
<th>Terms</th>
<th>Counterparty Credit Rating</th>
<th>Notional Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Pay-Fixed Interest Rate Swap</td>
<td>Hedge of changes in cash flows on the Series UU Bonds</td>
<td>5/3/2007</td>
<td>7/1/2029</td>
<td>Pay 4.08%; receive 67%</td>
<td>AA3/A+</td>
<td>$169,532</td>
</tr>
<tr>
<td>B</td>
<td>Pay-Fixed Interest Rate Swap</td>
<td>Hedge of changes in cash flows on the Series UU Bonds</td>
<td>5/3/2007</td>
<td>7/1/2029</td>
<td>Pay 4.08%; receive 67%</td>
<td>AA3/A+</td>
<td>$85,543</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Item</th>
<th>Type</th>
<th>Objective</th>
<th>Effective Date</th>
<th>Maturity Date</th>
<th>Terms</th>
<th>Counterparty Credit Rating</th>
<th>Notional Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$255,075</td>
</tr>
</tbody>
</table>

Derivative instruments A and B hedge changes in cash flows of the underlying bonds – floating rate notes with coupons based on 5-year SIFMA or 67% of 3-month LIBOR index, and maturities equal to the maturities of the corresponding swaps. As such they are considered hedging derivative instruments. As of June 30, 2015, the negative fair values of the derivative instruments are $51 million.

The following tables include summary information for the Authority’s effective hedges related to the outstanding swap agreements for fiscal year 2015.

<table>
<thead>
<tr>
<th>Instrument Type</th>
<th>Changes in Fair Value Classification</th>
<th>Amount</th>
<th>Fair Value at June 30, 2015 Classification</th>
<th>Amount</th>
<th>Notional</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest Rate Swap</td>
<td>Deferred Outflows</td>
<td>$(2,331)</td>
<td>Fair value of derivative instruments</td>
<td>$(51,195)</td>
<td>$252,875</td>
</tr>
</tbody>
</table>

**Interest-Rate Swap Agreements**

The terms and fair values of the outstanding interest-rate swaps as of June 30, 2015, were as follows (in thousands):

<table>
<thead>
<tr>
<th>Associated Power Revenue Bonds</th>
<th>Effective Date</th>
<th>Maturity Date</th>
<th>Fixed Rate</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Libor Bonds, Series UU</td>
<td>$ 169,532</td>
<td>3-May-07</td>
<td>1-Jul-29</td>
<td>4.08%</td>
</tr>
<tr>
<td>Muni-BMS Bonds, Series UU</td>
<td>$ 83,343</td>
<td>3-May-07</td>
<td>1-Jul-29</td>
<td>4.08%</td>
</tr>
<tr>
<td>Total</td>
<td>$ 252,875</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The notional amounts of the swaps match the principal amounts of the associated Power Revenue Bonds.

During fiscal year 2015, the payments of fixed rate interest from the Authority exceeded the amount received as variable interest rate from swap counterparties by $8.6 million.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  

June 30, 2015  

Using rates as of June 30, 2015, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term. These debt service requirements are included in the scheduled maturities of long-term debt disclosed further in this note. As rates vary, variable-rate bond interest payments and net swap payments will vary.

<table>
<thead>
<tr>
<th>Fiscal Year Ending June 30</th>
<th>Principal</th>
<th>Interest</th>
<th>Interest-Rate Swap, net</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(In thousands)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>$</td>
<td>2,108 $</td>
<td>8,209 $</td>
<td>10,317</td>
</tr>
<tr>
<td>2017</td>
<td>-</td>
<td>2,108 $</td>
<td>8,209 $</td>
<td>10,317</td>
</tr>
<tr>
<td>2018</td>
<td>-</td>
<td>2,108 $</td>
<td>8,209 $</td>
<td>10,317</td>
</tr>
<tr>
<td>2019</td>
<td>-</td>
<td>2,108 $</td>
<td>8,209 $</td>
<td>10,317</td>
</tr>
<tr>
<td>2020</td>
<td>-</td>
<td>2,108 $</td>
<td>8,209 $</td>
<td>10,317</td>
</tr>
<tr>
<td>2021-2029</td>
<td>252,875 $</td>
<td>18,973 $</td>
<td>73,882 $</td>
<td>345,730</td>
</tr>
<tr>
<td>Total</td>
<td>$252,875 $</td>
<td>29,513 $</td>
<td>$114,927</td>
<td>$397,315</td>
</tr>
</tbody>
</table>

As of June 30, 2015, the swaps had a negative fair value of approximately $51.2 million. The negative fair value of the swaps may be countered by a reduction in future net interest payments required on the variable-rate Power Revenue Bonds, creating higher synthetic rates.

As of June 30, 2015, the Authority was not exposed to credit risk because the swaps had a negative fair value. However, should interest rates change and the fair value of the swap become positive, the Authority would be exposed to credit risk in the amount of the derivative’s fair value. The swaps counterparties were rated A2 and Aa3 as issued by Moody’s Investors Service (Moody’s), AA- and A+ by Standard & Poor’s (S&P), and A and A+ by Fitch Ratings.

The derivative contract uses the International Swaps and Derivatives Association, Inc. Master Swap Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The Authority or the counterparties may terminate the swaps if the other party fails to perform under the terms of the contracts. Also, the swaps may be terminated by the Authority if the counterparties’ credit rating falls below Baal as determined by Moody’s or BBB+ as determined by S&P. If at the time of termination, the swap has a negative fair value, the Authority would be liable to the counterparty for a payment equal to the swap’s fair value.

The Authority and GDB entered into an agreement for a $100 million revolving line of credit to meet collateral posting requirements from the 2008 basis and interest rate swaps. As of June 30, 2015, there was a $35.1 million outstanding balance in this line of credit. This balance is mainly related to the amounts paid under the termination agreements of the swap.
Scheduled Maturities of Long-Term Debt

The scheduled maturities of long-term debt with interest thereon as of June 30, 2015, are as follows:

<table>
<thead>
<tr>
<th>Fiscal Year Ending June 30, 2015</th>
<th>Principal</th>
<th>Interest</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(In thousands)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2016</td>
<td>$1,192,767</td>
<td>$410,209</td>
<td>$1,602,976</td>
</tr>
<tr>
<td>2017</td>
<td>237,365</td>
<td>398,571</td>
<td>635,936</td>
</tr>
<tr>
<td>2018</td>
<td>249,535</td>
<td>387,096</td>
<td>636,631</td>
</tr>
<tr>
<td>2019</td>
<td>262,355</td>
<td>375,106</td>
<td>637,461</td>
</tr>
<tr>
<td>2020</td>
<td>275,275</td>
<td>362,190</td>
<td>637,465</td>
</tr>
<tr>
<td>2021-2025</td>
<td>1,597,350</td>
<td>1,595,571</td>
<td>3,192,921</td>
</tr>
<tr>
<td>2026-2030</td>
<td>1,853,485</td>
<td>1,192,077</td>
<td>3,045,562</td>
</tr>
<tr>
<td>2031-2035</td>
<td>1,410,080</td>
<td>752,836</td>
<td>2,162,916</td>
</tr>
<tr>
<td>2036-2040</td>
<td>1,429,730</td>
<td>373,869</td>
<td>1,803,599</td>
</tr>
<tr>
<td>2041-2043</td>
<td>568,785</td>
<td>60,643</td>
<td>629,428</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>9,076,727</td>
<td>5,908,168</td>
<td>14,984,895</td>
</tr>
</tbody>
</table>

Less:
- Unamortized discount and premium
  - Interest
  - Total long-term debt

<p>| | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>126,521</td>
<td>-</td>
<td>126,521</td>
</tr>
<tr>
<td></td>
<td>-</td>
<td>(5,909,010)</td>
<td>(5,909,010)</td>
</tr>
<tr>
<td><strong>Total long-term debt</strong></td>
<td><strong>9,203,248</strong></td>
<td></td>
<td><strong>9,203,248</strong></td>
</tr>
</tbody>
</table>

Current portion, net of discount and excess reacquisition costs
- of bonds
- Current portion of notes payable
- Total current portion
- Long-term debt, excluding current portion

|                                | (449,254)  | -         | (449,254)  |
|                                | (733,852)  | -         | (733,852)  |
|                                | (1,183,136) | -         | (1,183,136) |
| **Long-term debt, excluding current portion** | **8,020,142** | -         | **8,020,142** |

12. Employees' Retirement Benefits

Pension Plan

A. General Information about the Pension Plans

Plan Description

All of the Authority's permanent full-time employees are eligible to participate in the Authority's Pension Plan, a single employer defined benefit pension plan (the Plan) administered by the Employees' Retirement System of the Puerto Rico Electric Power Authority (the System). The System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report can be found in the following link: https://www2.aeepr.com/retiro/informes_financieros.html
If a member’s employment is terminated before he becomes eligible for any other benefits under this Plan, he shall receive a refund of his member contribution plus interest compounded annually. The Plan is not subject to the requirements of the Employees Retirement Income Security Act of 1974 (ERISA).

**Benefits Provided**

Benefit provisions under the Plan are established by the System’s regulation and Authority resolution. The System issues publicly available reports that include a full description of the pension plans regarding benefit provisions, assumptions and membership information that can be found on the System website.

Benefits include maximum retirement benefits of 75% of average basic salary (based on the three-highest annual basic salaries) for employees with 30 years of service; with reduced benefits, available upon early retirement. The Plan was amended on October 23, 1992 to provide revised benefits to new employees limiting the maximum retirement basic salary to $50,000. The plan was further amended in January 1, 2000 to provide improved retirement benefits to employees with 25 years or more of credited service. Disability and death benefits are also provided. Separation benefits fully vest upon reaching 10 years of credited service.

Supplemental benefits were unfunded and such benefits were reimbursed to the System when paid as of December 31, 1999. Effective January 1, 2000, the Board of Trustees of the System approved the transfer of the obligation for supplemental benefits provided by the Authority and funded through the System (supplemental pension obligations exchanged for forfeited sick leave benefits and the supplemental spousal survivor benefits) to the Retirement System. Also, the Board of Trustees of the System accepted an amortization period for the Plan of 40 years, which commenced on June 30, 1996.

The Authority’s employees with over 20 years of service are entitled to exchange accrued sick leave for supplemental pension benefits just to complete merit annuity (30 years of service) and/or be paid in cash the value of such sick leave upon separation from employment.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  

June 30, 2015  

The Plans’ provisions and benefits in effect as of June 30, 2015, are summarized as follows:  

<table>
<thead>
<tr>
<th>Hire date</th>
<th>Prior to January 1, 1993</th>
<th>On or after January 1, 1993</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benefit formula</td>
<td>75% @ 30 years of services at full retirement</td>
<td>75% is limited to $50,000 @ 30 years of services at full retirement</td>
</tr>
<tr>
<td>Benefit vesting schedule</td>
<td>10 years' service</td>
<td>10 years' service</td>
</tr>
<tr>
<td>Benefit payments</td>
<td>Monthly for life</td>
<td>Monthly for life</td>
</tr>
<tr>
<td>Retirement age</td>
<td>N/A</td>
<td>55</td>
</tr>
<tr>
<td>Monthly benefits, as a % of eligible compensation</td>
<td>Varies by age and years of services</td>
<td>Varies by age and years of services</td>
</tr>
<tr>
<td>Required employee contribution rates</td>
<td>9.06%</td>
<td>11.00%</td>
</tr>
<tr>
<td>Required employer contribution rates</td>
<td>34.54%</td>
<td>34.54%</td>
</tr>
</tbody>
</table>

_Employees Covered_  

As of June 30, 2015, the following membership were covered by the benefit terms for the Plan:  

<table>
<thead>
<tr>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td>Retired participants and beneficiaries currently receiving benefits</td>
</tr>
<tr>
<td>Terminated participants and beneficiaries entitled to benefits but not yet receiving benefits</td>
</tr>
<tr>
<td>Active participants</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

_Contributions_  

Article 5.2 of the System’s regulations require that the employer contribution rates be determined for the Authority on an annual basis by the actuarial valuation and shall be effective on the July 1 following notice of a change in the rate. Funding contributions for the Plan is determined annually on an actuarial basis as of June 30 by the System. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The Authority is required to contribute the difference between the actuarially determined rate and the contribution rate of employees. For the fiscal year ended June 30, 2015, the Authority's annual contribution was $1,553 million.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  
June 30, 2015  

B. Net Pension Liability  

The Net pension liability as of June 30, 2015 was measured as of June 30, 2014, and the actuarial valuation date was June 30, 2014. Changes in the Net Pension Liability for the year ended June 30, 2015 are presented below.  

Actuarial Assumptions  

The Authority recognizes annual Pension expense and Net pension liability in accordance with GASB Statements No. 68, “Accounting and Financial Reporting for Pensions” and GASB Statement No. 71 “Pension Transition for Contributions Made Subsequent to the Measurement Date” (using an annual actuarial valuation conducted by Cavanaugh Macdonald Consulting, LLC). A summary of principal assumptions and methods used to determine the net pension liability is shown below.  

The total pension liability measured as of June 30, 2014 was determined using the following actuarial assumptions:  

<table>
<thead>
<tr>
<th>Description</th>
<th>Assumption</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valuation Date</td>
<td>June 30, 2014</td>
</tr>
<tr>
<td>Measurement Date</td>
<td>June 30, 2014</td>
</tr>
<tr>
<td>Reporting date</td>
<td>June 30, 2014</td>
</tr>
<tr>
<td>Single Equivalent Interest Rate</td>
<td></td>
</tr>
<tr>
<td>Long-term expected rate of return</td>
<td>8.25%</td>
</tr>
<tr>
<td>Municipal Bond Index Rate</td>
<td>3.66%</td>
</tr>
<tr>
<td>Fiscal year in which Plan's</td>
<td></td>
</tr>
<tr>
<td>Fiduciary net position is projected to be depleted</td>
<td>2027</td>
</tr>
<tr>
<td>from future benefits payments for current members</td>
<td></td>
</tr>
<tr>
<td>Single Equivalent Interest Rate</td>
<td>4.27%</td>
</tr>
<tr>
<td>Actuarial Assumptions:</td>
<td></td>
</tr>
<tr>
<td>Discount Rate</td>
<td>4.27%</td>
</tr>
<tr>
<td>Inflation</td>
<td>2.5%</td>
</tr>
<tr>
<td>Payroll Growth</td>
<td>3.5%</td>
</tr>
<tr>
<td>Salary Increase</td>
<td>3.5% to 7.25%, including inflation</td>
</tr>
<tr>
<td>Investment Rate of Return</td>
<td>8.25%</td>
</tr>
<tr>
<td>Percentage Married</td>
<td>100% of employee, and wives are assumed to be 4 years younger than their husbands.</td>
</tr>
</tbody>
</table>

Mortality Assumptions  

(1) The mortality rates were based on RP-2000 Employee Mortality Projected to 2030 with Males set forward 5 years for actives and RP-2000 Combined Mortality Projected to 2030 with Males set back 1 year for inactive members.
Puerto Rico Electric Power Authority  
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Notes to Audited Financial Statements  
June 30, 2015

Participation

All employees participate. Each member participates under an optional regimen of benefits supplementary to or coordinated with Social Security. All members hired after September 30, 1990 can only participate in the supplementary scheme.

Compensation

Average of the three highest annual base salaries. For new members hired on or after January 1, 1993, annual compensation is limited to $50,000.

Merit Annuity

Eligibility: For members hired before January 1, 1993, 25 to 30 years of service. For members hired on or after January 1, 1993, there is a minimum age requirement of 55 years of age and 30 years of service. For this group, reduced benefits payable with less than age 55 are effective January 1, 2015.

Basic (Supplementary) Benefit: Life annuity of 2.5% of compensation times years of service up to 30.

Coordinated Benefit: Up to Age 65 = Basic (Supplementary) Benefit.  
After Age 65 = Basic (Supplementary) Benefit minus $40 for each year of service up to 30.

Maximum Benefit: 75% of compensation. The maximum is applied to all pensions paid by the System.

Accrued Benefit

Basic (Supplementary) Benefit: 1-1/2% of compensation for each year of service, plus 1/2% of compensation for each year of service after 20 years.

Coordinated Benefit:  
Up to Age 65 = Basic (Supplementary) Benefit.  
After Age 65 = Basic (Supplementary) Benefit minus $19 for each year of service up to 30.
Age Retirement

Eligibility: 60 years of age with at least 5 years of service.

Supplementary Pension: Life annuity of basic (supplementary) benefit.

Coordinated Pension: Life annuity of basic (supplementary) benefit until age 65 and coordinated benefit thereafter.

Actuarial Equivalent (Service) Retirement

Eligibility: 20 years of service.

Supplementary Pension: Immediate life annuity of actuarially equivalent value to basic (supplementary) benefit.

Coordinated Pension: Immediate life annuity of basic (supplementary) benefit until age 65 and of actuarially equivalent value to the coordinated benefit after age 65.

Actuarial Equivalent: Benefit of equivalent value to a deferred life annuity payable from age 60 on.

Separation Pension

Eligibility: Any age with at least 10 years of service.

Supplementary Pension: Deferred life annuity, payable at age 60, consisting of a basic (supplementary) benefit.

Coordinated Pension: Deferred life annuity, payable at age 60, consisting of a basic (supplementary) benefit until age 65 and of the coordinated benefit thereafter.

Disability Pension

Eligibility: Any age with at least 5 years of service (10 years of service if hired after December 31, 1992).
Regular Benefit: If eligible for a retirement pension or merit annuity, such applicable amount.

Alternative Benefit: If not eligible for a retirement pension or merit annuity, will receive:

⇒ Supplementary Pension = the greater of 90% of the basic (supplementary) benefit or 20% of Final Average Compensation.

⇒ Coordinated Pension:

Up to Age 65: Supplementary Pension Benefit.

After Age 65: Supplementary Pension Benefit minus $17.10 for each year of credited service. The resulting benefit cannot be less than 17.5% of Final Average Compensation.

**Death Benefit**

Benefit: Lump sum payment equal to the last salary at the time of retirement from active service or death in active service. The lump sum payment may be reduced in certain situations as described below.

Eligibility: Participants with all credited service with PREPA and age 60 with 15 years of credited service or under age 60 with 20 years of credited service at retirement date or death in active service.

Receive the full benefit. Members that comply with the age and service requirements have the option to receive payment while in active service. Members who elect to receive their death benefit early will have an increase in their employee contribution rate.

Retirees with age 60 and less than 15 years of service or under age 60 with less than 20 years of service.

The benefit will be based on a proportion of actual years of service and corresponding requirement of service according to age.

Retirees with combined credited service from PREPA and other government agency.

The benefit will be based on compensation from PREPA and the other government agency.
Disability with less than 5 years of service (10 years for members hired after December 31, 1992).

The benefit is proportionally reduced over 5 or 10 years depending on the hired date.

Survivor Benefit

The surviving spouses of retired members receiving a pension benefit will receive a life annuity equal to 30% of the annual pension payable to the member at the time of death.

Employee Contributions

Employee contributions are generally 9.06% of salary.

Employees who elect to receive prompt payment of their death benefit contribute 10.31% of salary if no additional death benefit is payable at retirement and 13.86% of salary if the increase in salary is payable at retirement. The employee pays the higher contribution rate from the time the early death benefit is paid until retirement. For new members, on or after January 1, 1993, employee contributions are 11% of salary.

For supplementary members said contributions are applied to the System. For coordinated members, the part equivalent to 4% of salary up to $4,200 is included as part of the employee contribution to Social Security, and the remainder is applied to the System.

Cost-of-Living Adjustment

A. Increase effective July 1, 1992 to all pensions granted on or before June 30, 1990 as follows:

1. 8% increase for the monthly pension up to $300.
2. 4% increase for the monthly pension between $300 and $600.
3. 2% increase for the monthly pension in excess of $600.

B. The minimum monthly increase will be $25 and the maximum $50.

C. Actuarial pensions will be granted the minimum increase of $25 per month if they were granted on or before June 30, 1990.
D. These increases, under the same conditions, will be granted automatically every three years beginning July 1, 1992 or from the retirement date for all those who retire after June 30, 1990.

**Annual Christmas Bonus**

Effective with the June 30, 2002 actuarial valuation, an annual $300 Christmas bonus is payable to all current and future retirees and beneficiaries.

Effective with the June 30, 2003 actuarial valuation, an additional annual $100 Christmas bonus is payable to all current and future retirees and beneficiaries, for a total of $400 per year.

**Summer Bonus**

Effective with the June 30, 2003 actuarial valuation, an annual $100 summer bonus is payable to all current and future retirees and beneficiaries.

**Funeral Benefit**

Effective with the June 30, 2004 actuarial valuation, a lump sum Funeral Benefit of $1,000 is payable to all current and future retirees.

**Note to Summary of Benefit Provisions**

The System became effective as of July 1, 1945 and includes the general fund for regular benefits among others. The valuation only covers the liabilities of the general fund.

Certain provisions of the Rules and Regulations are not described in the summary because of little applicability, for example, variations in formulas when annual compensation is below $5,000, or with respect to members whose service is before July 1, 1973. In general, if a member has the right to two comparable benefits, he will receive the greater, not both.

There are optional forms of pensions with actuarial adjustments. No additional cost is assumed with respect to optional benefits with actuarial adjustments. It is assumed that members severed before retirement will elect to leave their contributions in the System and will not elect to pay for the death benefit.
Discount Rate

The discount rate used to measure the total pension liability was 4.37%. The projection of cash flows used to determine the discount rate assumed that members contribute the mandatory contribution rate and the Employer will contribute the average employer contribution over the five-year period ended June 30, 2016, which is $93,867,922. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members until the plan year ending June 30, 2027. Therefore, the long-term expected rate of return on pension plan investments of 8.25% was applied to all periods of projected benefit payments through June 30, 2027 and the applicable municipal bond index rate of 3.73%, based on the S&P Municipal Bond 20 Year High Grade Rate Index as of June 30, 2015, was applied to all periods of projected benefit payments after June 30, 2027. The Single Equivalent Interest Rate (SEIR) of 4.37% that discounts the entire projected benefit stream to the same amount as the sum of the present values of the two separate benefit payments streams was used to determine the total pension liability as of June 30, 2015.

The long-term expected rate of return on pension System investments was determined using a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of pension System investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

Periods of projected benefit payments - Projected future benefit payments for all current System members were projected through 2134.

The target asset allocation and best estimates of arithmetic real rates of return for each major asset class as provided by the System's investment consultant for use in the last actuarial experience study, dated June 3, 2014 are summarized in the following table:

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Target Allocation</th>
<th>Long-Term Expected Real Rate of Return*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Loans</td>
<td>15.0%</td>
<td>4.35%</td>
</tr>
<tr>
<td>Internal Mortgages</td>
<td>5.0%</td>
<td>3.85%</td>
</tr>
<tr>
<td>Core Bonds</td>
<td>10.0%</td>
<td>2.87%</td>
</tr>
<tr>
<td>U.S. Large Cap Equity</td>
<td>22.0%</td>
<td>7.72%</td>
</tr>
<tr>
<td>U.S. Small Cap Equity</td>
<td>10.0%</td>
<td>8.97%</td>
</tr>
<tr>
<td>International Developed Equity</td>
<td>15.0%</td>
<td>8.43%</td>
</tr>
<tr>
<td>Emerging Market Equity</td>
<td>5.0%</td>
<td>9.19%</td>
</tr>
<tr>
<td>Long/Short Equity</td>
<td>8.0%</td>
<td>7.40%</td>
</tr>
<tr>
<td>Private Equity</td>
<td>5.0%</td>
<td>10.98%</td>
</tr>
<tr>
<td>Core Real Estate</td>
<td>5.0%</td>
<td>7.21%</td>
</tr>
<tr>
<td>Total</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

*Arithmetic mean
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Notes to Audited Financial Statements  
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C. Changes in the Net Pension Liability  

The changes in the Net Pension Liability for the Plan follows:  

<table>
<thead>
<tr>
<th>Increase (Decrease)</th>
<th>Total Pension Liability</th>
<th>Plan Fiduciary Net Position</th>
<th>Net Pension Liability/(Asset)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>($ in Thousands)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance at June 30, 2013</td>
<td>$ 3,043,512</td>
<td>$ 1,299,384</td>
<td>$ 1,744,128</td>
</tr>
<tr>
<td>Changes for the year:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Service cost</td>
<td>38,420</td>
<td>-</td>
<td>38,420</td>
</tr>
<tr>
<td>Interest</td>
<td>249,450</td>
<td>-</td>
<td>249,450</td>
</tr>
<tr>
<td>Differences between expected and actual experience</td>
<td>47,103</td>
<td>-</td>
<td>47,103</td>
</tr>
<tr>
<td>Changes in assumptions</td>
<td>1,796,904</td>
<td>-</td>
<td>1,796,904</td>
</tr>
<tr>
<td>Contributions - employer</td>
<td>-</td>
<td>100,145</td>
<td>(100,145)</td>
</tr>
<tr>
<td>Contributions - employee</td>
<td>-</td>
<td>36,871</td>
<td>(36,871)</td>
</tr>
<tr>
<td>Net investment income</td>
<td>-</td>
<td>179,191</td>
<td>(179,191)</td>
</tr>
<tr>
<td>Benefit payments, including refunds of employee contributions</td>
<td>(217,606)</td>
<td>(217,606)</td>
<td>-</td>
</tr>
<tr>
<td>Administrative expenses</td>
<td>-</td>
<td>(348)</td>
<td>348</td>
</tr>
<tr>
<td>Other Changes</td>
<td>-</td>
<td>1,274</td>
<td>(1,274)</td>
</tr>
<tr>
<td>Net changes</td>
<td>60,040</td>
<td>99,528</td>
<td>(39,488)</td>
</tr>
<tr>
<td>Balance at June 30, 2014</td>
<td>$ 4,957,783</td>
<td>$ 1,398,911</td>
<td>$ 3,558,872</td>
</tr>
</tbody>
</table>

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

The following presents the net pension liability of the System, calculated using the discount rate of 4.37 percent, as well as what the System’s net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (3.37 percent) or 1 percentage point higher (5.37 percent) than the current rate:
Puerto Rico Electric Power Authority  
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June 30, 2015

<table>
<thead>
<tr>
<th>(In thousands)</th>
<th>Miscellaneous</th>
</tr>
</thead>
<tbody>
<tr>
<td>1% Decrease</td>
<td>3.37%</td>
</tr>
<tr>
<td>Net Pension Liability</td>
<td>$4,263,885</td>
</tr>
<tr>
<td>Current Discount Rate</td>
<td>4.37%</td>
</tr>
<tr>
<td>Net Pension Liability</td>
<td>$3,603,802</td>
</tr>
<tr>
<td>1% Increase</td>
<td>5.37%</td>
</tr>
<tr>
<td>Net Pension Liability</td>
<td>$3,061,075</td>
</tr>
</tbody>
</table>

Pension Plan Fiduciary Net Position – Detailed information about each pension plan’s fiduciary net position is available in the separately issued Retirement System financial reports.

D. Pension Expense, Deferred of Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended June 30, 2015, the Authority recognized pension expense of $420.9 million. At June 30, 2015, the Authority reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

<table>
<thead>
<tr>
<th>In thousands</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred outflows of resources</td>
</tr>
<tr>
<td>Difference between expected and actual experience</td>
</tr>
<tr>
<td>Changes of assumptions</td>
</tr>
<tr>
<td>Employer contributions subsequent to the measurement date</td>
</tr>
<tr>
<td><strong>Total deferred outflows of resources</strong></td>
</tr>
</tbody>
</table>

Deferred inflows of resources

<table>
<thead>
<tr>
<th>In thousands</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net difference between projected and actual earnings on plan investments</td>
</tr>
<tr>
<td><strong>Total deferred inflows of resources</strong></td>
</tr>
</tbody>
</table>

Contributions of $100.9 million were reported as deferred outflows of resources resulting from contributions subsequent to the June 30, 2014 measurement date and will be recognized as a reduction in the net pension liability in the year ended June 30, 2016.
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The amounts reported as deferred outflows of resources (other than the contributions after the measurement date and before year end) and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

<table>
<thead>
<tr>
<th>Year Ended June 30</th>
<th>In thousands</th>
</tr>
</thead>
<tbody>
<tr>
<td>2016</td>
<td>377,916</td>
</tr>
<tr>
<td>2017</td>
<td>377,916</td>
</tr>
<tr>
<td>2018</td>
<td>377,916</td>
</tr>
<tr>
<td>2019</td>
<td>260,213</td>
</tr>
<tr>
<td>2020</td>
<td>-0-</td>
</tr>
<tr>
<td>Thereafter</td>
<td>-0-</td>
</tr>
</tbody>
</table>

Other Post-Employment Benefits (OPEB) 

Postemployment Health Plan 

Plan Description – PREPA Retired Employees Healthcare Plan (Health Plan) is a single-employer defined benefit healthcare plan administered by the Authority. During fiscal year 2010, the Authority adopted a resolution to change the Health Plan. The Health Plan for all retirees will be capped at $300 per member per month for retirees and spouses under age 65 and $200 per member per month for retirees and spouses age 65 and over.

Membership – During fiscal year 2010, the Health Plan changed to require all new retired employees on or after September 1, 2009, to have 30 years of service to receive health benefits. Certain retired employees on or after September 1, 2009, all retired employees before September 1, 2009, are eligible to participate in the Postretirement Health Plan. To remain eligible for participation, Medicare eligible retired participants and their spouses must enroll in Medicare Part B at age 65, or whenever eligible, at their own expenses. The benefit provisions to retired employees are established and may be amended by the Authority.

Funding Policy and Annual OPEB Cost – The required contribution is based on projected pay-as-you-go financing requirements. The contribution requirements of plan members and the Authority are established and may be amended by the Authority.

The Annual OPEB Cost is calculated based on the Annual Required Contribution (ARC) of the employer, an amount actuarially determined in accordance with the provisions of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is
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Projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years. The following table shows the components of the Authority’s annual OPEB cost for fiscal year 2015 (in thousands):

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual OPEB cost</td>
<td>$19,549</td>
</tr>
<tr>
<td>Actuarial Accrued Liability (AAL)</td>
<td>$378,444</td>
</tr>
<tr>
<td>Unfunded AAL</td>
<td>$378,444</td>
</tr>
<tr>
<td>Funded Ratio</td>
<td>0%</td>
</tr>
<tr>
<td>Annual Covered Payroll</td>
<td>$364,982</td>
</tr>
</tbody>
</table>

The net OPEB obligation change is as follows (in thousands):

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Change in net OPEB obligation:</td>
<td></td>
</tr>
<tr>
<td>Net OPEB obligation, beginning balance</td>
<td>$119,175</td>
</tr>
<tr>
<td>Total annual required contribution (ARC), July 1–June 30</td>
<td>18,754</td>
</tr>
<tr>
<td>Interest on Net OPEB obligation</td>
<td>4,767</td>
</tr>
<tr>
<td>Adjustments to annual required contribution</td>
<td>(3,972)</td>
</tr>
<tr>
<td>Actual benefit payments, July 1–June 30</td>
<td>(26,907)</td>
</tr>
<tr>
<td>Net OPEB obligation, ending balance</td>
<td>$111,817</td>
</tr>
</tbody>
</table>

For the fiscal year ended June 30, 2015, the Authority’s annual OPEB expense was $19.5 million. This expense is included in Administrative and General Expenses.

The Authority’s annual OPEB cost, and the net OPEB obligation for 2015 and the two preceding years were as follows:

<table>
<thead>
<tr>
<th>Fiscal Year Ended</th>
<th>Annual OPEB Cost</th>
<th>Percentage of Annual OPEB Cost Contributed</th>
<th>Net OPEB Obligation</th>
</tr>
</thead>
<tbody>
<tr>
<td>06/30/13</td>
<td>$20.5</td>
<td>113%</td>
<td>$119.8</td>
</tr>
<tr>
<td>06/30/14</td>
<td>$19.6</td>
<td>103%</td>
<td>$119.2</td>
</tr>
<tr>
<td>06/30/15</td>
<td>$19.5</td>
<td>103%</td>
<td>$111.8</td>
</tr>
</tbody>
</table>

**OPEB Actuarial Valuation** – The Authority’s other Post-Employment Benefits Program actuarial valuation was conducted by Cavanaugh Macdonald Consulting, LLC, Cavanaugh Macdonald Consulting, LLC is a member of the American Academy of Actuaries. The valuation was performed in accordance with GASB Statement No. 45 requirements.
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Actuarial Methods and Assumptions:

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actuarial Valuation Date</td>
<td>July 1, 2012</td>
</tr>
<tr>
<td>Actuarial Cost Method</td>
<td></td>
</tr>
<tr>
<td>Amortization method</td>
<td></td>
</tr>
<tr>
<td>Remaining Amortization Period</td>
<td>30 years</td>
</tr>
<tr>
<td>Actuarial Assets Valuation Method</td>
<td>Market Value of Assets</td>
</tr>
<tr>
<td>Investment Rate of Return</td>
<td>4% (includes inflation rate)</td>
</tr>
<tr>
<td>Inflation Rate:</td>
<td></td>
</tr>
<tr>
<td>Medical</td>
<td>3%</td>
</tr>
<tr>
<td>Prescription drug</td>
<td>Not applicable</td>
</tr>
<tr>
<td>Dental</td>
<td>4%</td>
</tr>
<tr>
<td>Projected Salary Increases</td>
<td></td>
</tr>
</tbody>
</table>

The required schedule of funding progress included supplementary information (Schedule 1) that presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

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

13. Revenues from Major Clients and Related Parties

Electric operating revenues from major clients and related parties are as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>(In thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Governmental sector, principally instrumentalities, agencies and corporations of the Commonwealth of Puerto Rico</td>
<td>$ 517,042</td>
</tr>
<tr>
<td>Municipalities of the Commonwealth of Puerto Rico</td>
<td>$ 231,792</td>
</tr>
<tr>
<td></td>
<td>$ 748,834</td>
</tr>
</tbody>
</table>

14. Net position

As of June 30, 2015, the Authority is in a net deficit position. The Authority faces a number of business challenges that have been exacerbated by the Commonwealth’s economic recession, the volatility in oil prices, and the fact that the Authority has not increased rates to its customers’ rates to levels sufficient to offset the effects of its rising costs. Its principal challenges, some of
which are interrelated, are: (i) addressing the decline in electric energy sales; (ii) addressing the volatility of oil costs; (iii) addressing high customer electric power rates; (iv) reducing government accounts receivables; and (v) improving its liquidity. In July 2014, the Authority entered into discussions with its financial stakeholders in an effort to stabilize the Authority’s liquidity situation and address its financial position. However, the Restructuring Support Agreement was subject to the approval of the Oversight Board under PROMESA, and the Oversight Board declined to approve the RSA on June 27, 2017. As a result, the RSA terminated by its own terms on June 29, 2017. On June 30, 2017, the Governor submitted a letter to the Oversight Board stating that the Authority desired to effect a plan to adjust its debts under Title III of PROMESA as a result of the rejection of the RSA and the lack of a stay under PROMESA. On July 2, 2017, the Oversight Board filed a petition under Title III of PROMESA in the United States District Court for the District of Puerto Rico, commencing a Title III case for the Authority. See further discussion in Notes 19 and 20.

15. Contribution in Lieu of Taxes and others

(In thousands)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contribution in lieu of taxes</td>
<td>$229,633</td>
</tr>
<tr>
<td>Other appropriations</td>
<td>43,827</td>
</tr>
<tr>
<td>Total</td>
<td>$273,460</td>
</tr>
</tbody>
</table>

16. Commitments and Contingencies

Environmental Matters

Facilities and operations of the Authority are subject to regulation under numerous Federal and Commonwealth environmental laws, including the Clean Air Act, Clean Water Act, Oil Pollution Act (OPA), Resource Conservation Recovery Act (RCRA), Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and Underground Storage Tanks, among others.

In February 1992, the Environmental Protection Agency (EPA) conducted a multimedia inspection of the Authority’s facilities and identified several alleged instances of noncompliance related to the Authority’s air, water and oil spill prevention control and countermeasures compliance programs.
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The Authority and the EPA negotiated to resolve the issues regarding the deficiencies observed during the inspection and to ensure future compliance with all applicable laws and regulations. As a result of the negotiations, the Authority and the EPA reached an agreement that resulted in a consent decree (the Consent Decree) approved by the United States federal court in March 1999. Under the terms and conditions of the Consent Decree, the Authority paid a civil penalty of $1.5 million, and implemented additional compliance measures amounting $4.5 million. In addition, the Consent Decree requires that the Authority improve and implement compliance programs and operations in order to assure compliance with environmental laws and regulations.

In 2004, the United States federal court approved a modification to the Consent Decree agreed by the Authority and the EPA under which the Authority reduced, in two steps, the sulfur content in the No. 6 fuel oil used in certain generating units of its Costa Sur and Aguirre power plants (to 0.75% or less by March 1, 2005 and to 0.5% or less by March 1, 2007), and used No. 6 fuel oil with sulfur content of not more than 0.5% through July 18, 2009 at its Palo Seco and San Juan power plants. Additionally, the Authority has completed a nitrogen oxide emissions reduction program and modified the optimal operating ranges for all its units under the Consent Decree. The Authority also paid a $300,000 civil fine and reserved $200,000 to fund certain supplemental environmental projects and programs under the Consent Decree.

PREPA has audited several instances for compliance with the Consent Decree programs, and understands that a considerable number of them can be closed since their requirements have been completed. PREPA has formally requested to meet with EPA on August 20, 2010; February 25, 2011; May 23, 2012 and June 15, 2012 to begin the process conducive to the partial termination of certain provisions of the Consent Decree and its Modification. On July 22, 2014, representatives from PREPA, EPA and United States Department of Justice (DOJ) met to begin the discussion towards the termination of some of the programs. As a result, the EPA and the DOJ requested PREPA to submit information regarding PREPA’s compliance with the Programs for their review and evaluation. On September 25, 2014, PREPA met again with EPA and DOJ representatives and submitted the information requested, along with a letter where PREPA formally requested the EPA to review and approve the termination of those programs/provisions of the Consent Decree and its Modification of 2004 presented, as well as begin the process toward jointly filing in the Court a stipulation for Partial Termination of such programs.

To accomplish this goal, PREPA suggested to appoint a task force composed of EPA and PREPA representatives to schedule and meet to address the details which EPA Agreed to. As of March 2015, task force meetings between PREPA and EPA have not been scheduled, pending PREPA’s compliance with Mercury and Air Toxic Standards (MATS) future talks.
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Since September 2004, there has been no legal action in the United States federal court or any administrative proceeding against the Authority regarding the Consent Decree or its modification. The Consent Decree includes stipulated penalties for certain events of noncompliance. Noncompliance events must be disclosed to EPA in the corresponding report. Ordinarily, when a covered noncompliance event occurs, the Authority pays the stipulated penalty in advance in order to benefit from a 50% discount of the applicable stipulated penalty.

Other Proceedings

In 1997, as a result of an inspection carried out by the EPA and the Puerto Rico Environmental Quality Board (the EQB) at the Authority’s Palo Seco power plant, the EPA issued an Administrative Order for the investigation and possible remediation of seven areas identified by the EPA at the Palo Seco power plant and the Palo Seco General Warehouse (Depot). The Administrative Order required the Authority to carry out a Remedial Investigation/Feasibility Study (RI/FS). The RI/FS required under the order was designed to: (1) determine the nature and extent of contamination and any threat to the public health, welfare or environmental caused by any release or threatened release of hazardous substances, pollutants, or contaminants at or from the site; and (2) determine and evaluate alternatives for the remediation or control of the release or threatened release of hazardous substances, pollutants, or contaminants at or from the site. The RI was completed, and a final report was submitted to EPA for evaluation. The information gathered under the RI reflected the presence of free product (Separate Phase Hydrocarbons) in several monitoring wells. The analysis of this product also reflected a low concentration of polychlorinated biphenyls (PCBs). PREPA and EPA entered into an Administrative Order Consent (AOC) (CERCLA0220082022) requiring the Authority to complete a removal plan that consisted of determining if the underground water had been impacted by PCBs, the extent of the contamination and the implementation of a work plan for free product removal. Analytical data collected during this activity reflected that underground water had not been impacted by PCBs. Nevertheless, water/oil mix was found in seven monitoring wells (MWs). PCBs concentrations between 1.36-2.36 parts per million were detected in the oil found in 3 of the 7 MWs. Multiphase extraction (MPE) activities in the MWs where water/oil phases were found, has been performed on a weekly basis. After several MPE, this activity was discontinued under the USEPA’s recommendations.

On April 19, 2012, FREPA submitted for EPA’s review and approval the final report letter for the AOC. On August 13, 2012, EPA notified PREPA by certified mail, that the final report was reviewed and determined that the work required pursuant the AOC has been fully carried out in
accordance with its terms. Also, the letter indicated that the notification shall not affect any continuing obligation of respondents, including but not limited to the reimbursement of EPA response costs, as specified in the AOC.

Based on the findings of the RI, the Human Health Risk Assessment, the Screening Level Ecological Risk Assessment and the AOC, NO ACTION recommendation under CERCLA for the PREPA Palo Seco site is believed to be protective of human health and environment. The risk assessments indicate that the levels of residual contaminants present at the site fall within EPA’s acceptable risk range. This nonaction remedy complies with the federal and commonwealth requirements.

“Both Orders” with both AOC’s established a Reimbursement of Costs condition in which the Authority agreed to reimburse EPA for all costs incurred by EPA in connection to the site. Since the time EPA began its investigation in 1992, EPA alleges that it incurred response costs totaling approximately $1,535,138.93, which include both direct and indirect costs.

On September 21, 2015, PREPA and the United States entered into a tolling agreement (“Tolling Agreement”), which specified that the period commencing on September 21, 2015 and ending on July 21, 2016 is not to be included in computing the period of time that the United States has to initiate a lawsuit for response costs. In the Tolling Agreement, PREPA reserves all rights and defenses which it may have, including the running of any statute of limitations.

On March 7, 2016, EPA sent PREPA a bill for $62,077.31, which represented the cost of the work required under the Consent Order (which PREPA was contractually required to pay EPA under the terms of the Consent Order). PREPA submitted to the United States the full payment of $62,077.31.

On May 11, 2016, EPA sent PREPA a detailed cost package for the remaining response costs (i.e., these not directly related to the Consent Order) it claims is owed spanning from 1996 to 2015, which total $1,473,061.62. On July 7, 2016, EPA and PREPA signed a First Amendment to the Tolling Agreement to extend initial the Tolling Period until January 21, 2017.

PREPA has reviewed the full cost package provided by EPA and the negotiations continue until PREPA and EPA agree to terms on a settlement. The length of the negotiation process will depend on PREPA’s settlement offer and EPA’s willingness to compromise.

In 2002, the Authority received a “Special Notice Concerning Remedial Investigation/Feasibility Study for Soil at the Vega Baja Solid Waste Disposal Superfund Site. The EPA has identified the Authority and six other entities as “potentially responsible parties”, as defined in the CERCLA.
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In 2003, the Authority agreed to join the other potentially responsible parties in an Administrative Order on Consent (AOC) for an RI/FS, with the understanding that such agreement did not constitute an acceptance of responsibility. Under the AOC, the Authority committed up to $250,000 as its contribution to partially fund the RI/FS. At this time, RI/FS has been completed. The work proceeded in accordance with the schedule established by the Authority and the other designated potentially responsible parties. On July 2010, a proposed plan was issued identifying the Preferred Alternative to address soil contamination at the Vega Baja Solid Waste Disposal Site. EPA held a public hearing on August 3, 2010 to discuss the alternatives to address soil contamination. 

The Record of Decision (ROD) was published as scheduled by EPA on September 30, 2011. Alternative No. 2, Removal with OnSite Consolidation and Cover in the NonResidential Area, was selected. From this point on, EPA resumed negotiations with the Potential Responsible 16 Parties (PRP’s), both private and public, towards signing a Consent Decree through which the PRP’s would contribute enough funds to cover the costs of the remedial action and the maintenance of the site. PREPA has already approved a contribution of $1,000,000 through Resolution 3804, April 1, 2011. Notwithstanding, through further negotiations an additional contribution of $300,000 was required by EPA. This additional contribution was approved by PREPA’s Governing Board. 

On December 4, 2012, the Federal Department of Justice lodged with the Court the Consent Decree (CD) Civil Action No. 3:12cv01988, which requires that PREPA shall pay to EPA for the Past Response Costs of the agency the amounts of $300,000 within 30 days of the effective date; $300,000 not later than August 15, 2013 and $300,000 not later than August 15, 2014. In accordance with the definition of “effective date” in the CD, is the day the decree is entered on the court’s docket controls. The Federal Court signed the CD on April 19, 2013 and entered the CD on the Docket on April 25, 2013. PREPA has complied with the Past Response Cost payment provided in the CD. The CD also establishes that PREPA shall pay to EPA all Future Response Cost not inconsistent with the National Contingency Plan. PREPA has not been charged for these costs and therefore there is no amount recorded in the financial statements for these cost reimbursements. 

On April 10, 2013, an Environmental Escrow Agreement (EEA) was entered into by and among the Government Development Bank for the Puerto Rico, as the escrow agent, the Puerto Rico Land Authority, the Puerto Rico Housing Department and PREPA; and the United States of America on behalf of the Environmental Protection Agency. This agreement became effective on
April 25, 2013. The EEA (Account No. 25103952) was created to serve as financial assurance for the performance of the obligation under the CD. On June 24, 2013, PREPA deposited $400,000 into the escrow as provided in the CD.

As agreed by the parties, this CD can be terminated upon motion by any party, provided that all public Defendants have satisfied their obligations of payments of Response Cost and Stipulated Penalties. Termination of this Consent Decree shall not affect the Covenants Not to Sue (Sections XX and XXI of the CD) including all reservations pertaining to those covenants and shall not affect any continuing obligation of the Settling Defendants under sections IX, X, XVI, XXIII and XXIV of the CD.

Construction and Other Commitments

As of June 30, 2015, the Authority has commitments of approximately $48 million on active construction, maintenance and engineering services contracts.

Compliance Programs

The Authority continues to develop and implement a comprehensive program to improve environmental compliance in all applicable environmental media. This program has been and continues to be updated to conform to new regulatory requirements.

Air Quality Compliance

The Authority is consistently maintaining a 99% or better level of compliance with in stack opacity requirements. The Authority continues to use No. 6 fuel oil with sulfur content of 0.5% or better in its San Juan, Palo Seco and Aguirre Power Plants. In the case of the South Coast power plant, Units 5 and 6 have been converted to use natural gas, and are currently operating on a dualfuel scenario. Units 3 and 4 operate minimally, and use Bunker C as fuel oil.

Mercury and Air Toxics Standards (MATS)

The Mercury and Air Toxics Standard (MATS) was published by the EPA, pursuant to Section 112 of the Clean Air Act (CAA), to establish national emission standards for hazardous air pollutants (NESHAP) limits and work practice standards for pollutants emitted from coal and oil fired electric utility steam generating units (EGU). It became effective on April 16, 2012, sixty days after it was published as a Final Rule in the Federal Register, Vol. 77, No. 32 on February 16, 2012.
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The requirements established by the MATS are found in the Code of Federal Regulations, Title 40, Part 63, Subpart UUUU, National Emission Standards for Hazardous Air Pollutants from Coal and Oil Fired Electric Utility Steam Generating Units. The terms and definitions used in this regulation are included in 40 CFR 63.10042, Subpart UUUU. The MATS applies to new, reconstructed or existing coal and oilfired EGUs in continental and non-continental areas (from industry, federal government, state and tribal government). In the case of Puerto Rico, there are fourteen (14) oilfired EGUs affected by the regulation, which are operated and maintained by the PREPA, and two (2) coalfired EGUs which are operated and maintained by AESPuerto Rico, L.L.P.

The new rule requires that the affected units comply with the new standard requirements by April 16, 2015. According to MATS, owners/operators of units that cannot comply by the initial compliance date of April 16, 2015 can request an additional year (1st year) from the local environmental regulatory agency. In Puerto Rico, according with section 112(i)(3), of the CAA, the EQB has the delegated authority to approve such extension. Owners and operators can also request a second year (2nd year) extension to the EPA for those units that are determined to be critical to the reliability of the electrical system. This is based on the EPA’s Enforcement Policy for Use of Clean Air Act Section 113(a) Administrative Orders in Relation to Electric Reliability and the Mercury and Air Toxics Standard of December 16, 2011. In order to obtain the second-year extension, an early notice of compliance plans must be filed with the local Planning Authority (The Puerto Rico Planning Board) by April 16, 2013, a year after the effective date of the rule.

MATS Compliance Strategy

Pursuant to Section 112(1)(3) of the Clean Air Act, PREPA initiated the process for requesting an Administrative Order for some of the EGUs affected by the MATS and to obtain from the EPA a 2nd year extension to the MATS initial compliance date for such units determined to be critical for the reliability of Puerto Rico’s electrical system. On April 16, 2013, PREPA submitted an Early Notice of Compliance Plan to the Puerto Rico Planning Board. On May 14, 2013, the Governor of Puerto Rico issued an Executive Order (No. 2013-040) to create an Electrical Reliability Council, whose main goal is to evaluate the impact of the MATS implementation strategies and the integration of renewable energy source projects on the Puerto Rico’s electrical system’s operation and reliability. The Council creation became necessary because Puerto Rico is not subject to NERC or FERC jurisdiction. This Council would also serve as the Technical Advisor to the Puerto Rico Planning Board regarding PREPA’s claim of the critical reliability impact of the EGUs included in the Early Notice of Compliance Plan.
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PREPA has developed and commenced the implementation of this compliance plan for the new MATS emission limit requirements, as well as to address compliance with future air compliance regulations. Continuous compliance of some of the existing applicable units with MATS and future air compliance regulations requires the construction and development of a natural gas supply infrastructure in the Island of Puerto Rico. Unlike the Continental United States, this infrastructure is currently extremely limited to one port in the south side of the Island with no transmission and distribution pipelines. If natural gas is to be a viable option, infrastructure needs to be developed to supply some of PREPA’s existing EGUs and any new future generation units.

The development and construction of such infrastructure will result in the delay of the installation of controls (conversion projects) at some of the selected PREPA’s existing EGUs, some of which require the EQB to grant a 1st year extension of the MATS initial compliance date of April 16, 2015. Such delays also affect other existing EGUs that are critical to the Puerto Rico’s isolated electrical grid reliability.

In the case of Costa Sur Units 5 and 6, the EGUs were converted to use natural gas and bunker C in a dual fuel scenario 2011. Under MATS classification, they have been designated as Non-Continental Liquid Oil-Fired EGUs. The infrastructure to supply natural gas to these EGUs is in the EcoEléctrica’s Liquefied Natural Gas terminal located in Peñuelas. To comply with the MATS, PREPA elected the filterable particulate matter (PM) parameter and installed PM continuous monitoring systems in both units. Costa Sur 5 & 6 are in full compliance with the PM limitation and has also complied with the required notification and reporting requirements. It has also complied with the tune up requirement and the water content in fuel requirement.

Units 3 and 4 were designated as Limited-Use Liquid Oil-Fired EGUs, which entails limiting each unit’s operation to less than 8% in a 24 months block period of their respective nameplate heat input capacity, effective on April 16, 2015. These units are in compliance with the limited use, notification, tune up requirements and water content in fuel requirement.

For the Aguirre Power Complex Units 1 and 2, they will be designated as Natural Gas-Fired EGUs upon completion of their respective conversion projects to provide them with the capacity to use natural gas as the primary fuel. Under this category, these EGUs will not be subject to MATS. To supply natural gas to the units, PREPA is committed to contract the development of the AOGP with Excelerate Energy, LLC, which is the contractor chosen to develop, construct and operate this gas port. The gas port will be located approximately 3 miles offshore the Jobos Bay in the municipality of Salinas, within the southern shore of the Commonwealth of Puerto
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Rico’s territorial waters. The floating LNG terminal comprises an LNG transfer platform, a floating storage and regasification unit (FSRU), and a 4.1-mile-long submarine natural gas pipeline. LNG will be received through LNG carriers that will dock in the terminal’s platform.

This project is still in the process of obtaining the required regulatory certifications, endorsements, approvals, and permits from the agencies with jurisdiction (EQB, FERC and OGPe, among others) prior to commencing its construction. PREPA is in conversations with EPA regarding MATS compliance at Aguirre, since the unit’s conversion and gas port construction has been delayed beyond what was originally expected.

On the Early Notice of Compliance Plan presented to the Puerto Rico Planning Board and EPA, PREPA presented the conversion of the San Juan Units 9 and 10 and Palo Seco Units 3 and 4 as the compliance strategy to follow. Since this strategy requires a source of natural gas, and no source is currently available, PREPA is in conversations with EPA regarding MATS compliance in Palo Seco and San Juan.

For the rest of the applicable EGUs (San Juan Units 7 and 8, and Palo Seco Units 3 and 4), they were designated as Limited Use Liquid OilFired EGUs, which entails limiting each unit’s operation to less than 8% in a 24 months block period of their respective nameplate heat input capacity, effective on April 16, 2015. These units are also included in PREPA’s conversations with EPA, since they were used beyond the rule requirements for limited use units in order to maintain the electrical system’s stability and reliability.

*QA/QC Continuous Monitoring Program*

This program requires quarterly audits to the opacity monitors in PREPA’s power plants to insure compliance with the Consent Decree Clean Air Compliance Program. Also, this program requires annual quality assurance audits to the optimization monitors at our power plants in compliance with the Consent Decree. All these reports have been performed and submitted in compliance with the Consent Decree stipulations.

*Relative Accuracy Test Audit (RATA)*

A Relative Accuracy Test Audit (RATA) is a test to validate and certify for a period of one year the plant’s Continuous Emission Monitoring Systems (CEMS) equipment for purposes of continuous data collection. The requirements to perform this test are found at 40 CFR Part 60
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Appendix F and is to insure compliance with the Plants PDS air operation permits. Annually reports have been performed and submitted in compliance with the air operation permits requirements. *Title V Permitting Program.*

The Environmental Quality Board issued final permits for Palo Seco and Aguirre Power Plants on March and April 2015, respectively. PREPA is still awaiting issuance of a Title V for the San Juan Power Plant, Costa Sur Power Plant, Mayaguez, Cambalache, Daguao, Jobos and Vega Baja turbines. All the requested information has been submitted. Permit renewal application for the Yabucoa Turbine Power Block is dated December 14, 2016, Permit shield granted on January 18, 2017. Final permit approval is pending at PREQB.

*Water Quality Compliance*

As of December 2010, the Authority had achieved and has maintained a level of compliance with the Clean Water Act regulations (NPDES permits, Safe Drinking Water Act, OPA’90 (FRP’s and Operations Manual) and SPCC Regulation) in excess of 99%. The Authority has completed compliance plans for abating water pollution at its four major power plants Aguirre, San Juan, South Coast, and Palo Seco, as required by the Consent Decree, Section VI, Part I.

PREPA prepared and submitted the San Juan Power Plant and the Aguirre Power Complex NDPES Renewal Applications on September 30, 2011 and June 30, 2015, respectively. In compliance with the regulatory requirement, PREPA submitted it 180 days before the current NDPES Permits expiration dates. The current NPDES Permit are administratively extended until the EPA grants a renewed permit. PREPA uses drinking water from the Puerto Rico Aqueducts and Sewer Authority (PRASA) as raw water in order to generate electricity at the San Juan Power Plant. In 1994, Puerto Rico experienced a prolonged drought that forced PRASA to implement a water rationing plan, which limited the operation of the San Juan generating units.

In addition, this power plant has exceedances related to the NPDES Discharge Permit (National Pollutants Discharge Elimination System) PR0000698. Specifically, with Outfalls 002 and 003 permit limit exceedances. The issuance of a new NPDES permit for SJPP in 2007 and a Water Quality Standards Regulation revision from the EQB in 2003 imposed more restrictive permit limits, which eventually led to the issuance of an Administrative Order (AO) CWA-02-2010-3119 by the EPA. As a control measure, PREPA developed the San Juan Waste Water Treatment
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Plant Improvement project (PREQB Project No. C7209640) approved by the State Revolving Fund, that currently is under construction. The main purpose of this project is the reuse of the Outfalls 002 and 003 processes wastewaters, leaving these discharges as storm water only.

In April 2016, PREPA substantially completed the Phase I of the San Juan Waste Water Treatment Plant Improvement Project. This phase consists of the reuse of the generating units' feedwater heaters condensations. Phase IV that consists of the acquisition and installation of Microfiltration and Reverse Osmosis Systems is in the contract signing process. PREPA's power generation, especially steam power plants, requires the high volumes of water. In the case of the Aguirre Power Complex (APC), this water comes from a water well system owned and operated by PREPA. These water wells supply capacity has been reduced throughout the years due to urban expansion in the Salinas Municipality, causing salt water intrusion to the aquifer. Considering this, PREPA determined to develop and construct the necessary infrastructure to supply raw water from the Patillas Irrigation Channel to the APC, keeping the current well water supply as backup. The raw water will then be treated in the APC using ultrafiltration, reverse osmosis and demineralization methods. Also, the project provides for the reuse of condenser cooling water that is currently discharged thru the APC Outfalls, under the National Pollutant Discharge Elimination System Permit Program (NPDES Permit Program) required by Title 40 of the Code of Federal Regulations, Part 122.

PREPA already completed the Phase II (Filtration System Building) in March 2015 of the Water Supply Project from the Patillas Irrigation Channel. Phase III (Retention Ponds Construction) of this project have an 86% of completion and Phase I (Pipeline Construction from the Irrigation Channel) is the bid process. Phase IV (Pipeline interconnections inside the plant and water treatment equipment acquisition) is in a prebid process.

For the financing of the San Juan Waste Water Treatment Plant Improvement (C-72-096-40) and the Water Supply Project from Patillas Lake Irrigation Channel Projects (C-72-128-19), PREPA signed two Loan Agreements at 2% interest rate, pursuant to the Commonwealth of Puerto Rico Water Pollution Control State Revolving Fund Program (SRF Program). The first one was signed on September 6, 2012 for the amount of $17,560,028 and the second one on September 27, 2013 for the amount of $9,463,258.00. The September 27, 2013 agreement included a Grant for the amount of $1,536,742. These projects were not included in the PREPA's Capital Improvement Plan.
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Since 1977, PREPA submitted to EPA an updated request under Section 316(a) of the Clean Water Act that its South Coast power plant be permitted to discharge into the Caribbean Sea heated sea water that was previously used for cooling purposes, as part of the plant’s combustion and generation process, known as “thermal effluent”. EPA denied a 316(a) Thermal Variance Request in December 2000. After several discussions and meetings, EPA and PREPA agreed to perform a Detailed Engineering and Environmental Review (DEER) of alternatives to select a final alternative for the cooling water discharge that meets the water temperature standard or otherwise, qualify for a waiver request under Section 316(a) of the Water Quality Act. While the DEER was in progress EPA issued a draft permit for the power plant, which included a compliance schedule for the DEER selected alternative (Offshore Submerged Discharge – OSD).

The selected alternative estimated capital cost was approximately $60 million. EPA issued a final permit in October 1, 2009 with a schedule of compliance for relocation of Outfall 001. PREPA submitted the scoping document, an inventory of the environmental studies already performed and a Joint Permit Application for the Outfall 001 relocation in December 2009. As part of the permit requirements, PREPA prepared a Preliminary Environmental Impact Statement (PEIS) including the discussions of four alternatives for the 001 Outfall by October 2011. The PEIS included an incove alternative to reduce the cooling water discharge temperature to a thermal tolerance temperature range based on operations improvements and partial restoration of the historic flow. On January 30, 2013, PREPA submitted a Final Environmental Impact Statement (FEA) at the Puerto Rico Management Permits Office (OGPe) including the incove alternative, as the preferred one. The FEA was approved by the OGPe on August 5, 2013.

PREPA prepared and submitted the South Coast Power Plant NDPES Renewal Application on March 28, 2014. In compliance with the regulatory requirement, PREPA submitted the application 180 days before the current NDPES Permit expiration date (September 30, 2014). The current NPDES Permit is administratively extended until the EPA grants a renewed permit.

As part of the NPDES permit renewal, PREPA included OGPes’s determination that the incove is the less environmental impact activity according to Article 4(b)(3) of the Environmental Public Policy Act [Act 416 – 2004].

EPA included, as part of Section 316(a) requirements in the current San Juan Power Plant NPDES Permit, the performance of thermal plume studies and the biological monitoring program. PREPA submitted the thermal plume study plan and the QA/QC Plan for the Biological Monitoring Program in March 13, 2009, and it is waiting for EPA approvals. Also, EPA included, as another compliance requirement, the performance of a Comprehensive
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Demonstration Study (CDS) under the Section 316(b) of the Clean Water Act. On March 31, 2008, PREPA submitted an Impingement and Entrainment Characterization Study and Current Status Report for EPA evaluation. Also, PREPA submitted a Postrepowering Verification Study Work Plan for 316(b) in June 30, 2008 and it is waiting for EPA approval. PREPA made a reference of all the above mentioned pending work plans approvals and 316(b) reports at the San Juan Power Plant NDPES Renewal Application submitted to EPA on September 30, 2011. EPA has not responded to this petition yet.

Proposed Regulation under the CWA

Pursuant to a consent decree with environmental organizations, the EPA has issued past rulemaking under Section 316(b) of the CWA in three phases. Existing large electricgenerating facilities were addressed in Phase II of the rulemaking which was finalized in February 2004, while the existing small electricgenerating and all manufacturing facilities were addressed in Phase III of the rulemaking, which was finalized in June 2006. However, the Phase II rulemaking and a portion of the Phase III rulemaking were subject to legal challenges and, therefore, remanded to EPA for reconsideration. As a result, on April 20, 2011, EPA published a new draft rule pertaining to Section 316(b) of the CWA. Compliance with this rule is established in reference to the date of issuance of the final rule. According to the terms of a settlement agreement with Riverkeeper, EPA was required to issue the final rule by July 27, 2012. The final rule was not issued by EPA at the proposed date, but instead signed an agreement with Riverkeeper (the “Third Amendment”) to finish the rule by November 4, 2013. EPA issued the 316 (b) Final Rule on November 12, 2014.

This new regulation has three (3) components. First, existing facilities that withdraw at least 25 percent of their water from an adjacent water body, exclusively for cooling purposes, and have a design intake flow of greater than 2 million gallons per day would be subject to an upper limit on the amount of fish allowed to be affected by impingement. To comply with this requirement, each facility is given the option of selecting the technologies that would be best suited to address it or reduce its intake velocity to 0.5 feet per second. Second, existing facilities that withdraw very large amounts of water, at least 125 million gallons per day, would be required to conduct studies to help their permitting authority determine whether and what sitespecific controls, if any, would be required to reduce the number of aquatic organisms sucked into cooling water systems, known as entrainment. Third, new units that add electrical generation capacity at an existing facility would be required to add technology that is equivalent to closedcycle cooling which may be achieved by incorporating a closedcycle system into the design of the new unit or making other design changes with equivalent results.
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PREPA has developed and is in the process of implementing an impingement and entrainment control technology (Aquatic Filter Barrier) in its South Coast Power Plant. This technology includes the verification sampling for impingement and entrainment. On June 1, 2011, PREPA prepared and submitted to EPA a Plan of Action ("POA") for the South Coast Power Plant. The POA recommends the steps required to achieve the impingement and entrainment reduction. Based on these steps, PREPA understands that it will be able to comply with the existing NPDES permit conditions. In January 2015, PREPA finished the installation of an Aquatic Barrier at Units 5 and 6 Intake Structure, according with the compliance alternatives included in the EPA’s POA. Also, PREPA installed a Hydrolox Traveling Screen in the Unit 6 Intake Area. PREPA performed verification sampling for impingement and entrainment at the Units 5 and 6 Intake Area.

*Underground Injection Control Regulation*

PREPA has prepared a compliance plan to comply with the EQB’s underground injection control regulations. This plan entails the closing of certain septic systems where sanitary discharges can be connected to the Puerto Rico Aqueduct and Sewer Authority (PRASA) system. As of December 2014, the projects at San Juan, Aguirre, Palo Seco, and South Coast Power Plants for the connection of the sanitary discharges to the PRASA system have been completed. PREPA completed the sampling and analysis of the septic systems at Aguirre. Palo Seco is in the process of preparing specifications for the bid of the system closings. For the San Juan Power Plant the EQB’s asked to perform a Contamination Extension Plan.

*Spill Prevention Control and Countermeasures Plan (SPCCP)*

Under Section 311 of the CWA, EPA has issued regulations setting forth requirements for prevention of, preparedness for, and response to oil discharges at specific nontransportation related facilities. To prevent oil from reaching navigable waters and adjoining shorelines, and to contain discharges of oil, the regulation requires these facilities to develop and implement SPCC Plans, and establishes procedures, methods and equipment requirements.

Pursuant to the terms of the Consent Decree, PREPA was required to implement a Spill Prevention Maintenance and Construction Program (SPMCP). This program included major overhauls to dike and fuel tanks. As of December 2009, the Authority completed all compliance projects under the SPMCP of the Consent Decree, in accordance with the established scope of work.
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PREPA has a program to comply with new SPCC requirements, which became effective on November 10, 2011. These requirements addressed the containment of potential leakages from oil containing electrical equipment in its distribution substations. PREPA has already implemented the monitoring and inspection requirements under these new regulations (40 C.F.R. §112.7(k)). Notwithstanding, during fiscal year 2011, PREPA completed the installation of spill response material at all its substations. In addition, it completed the construction of secondary containment at 36 of the 54 substations that are located besides water bodies. PREPA has budgeted $1.5 million for the completion of this program.

During 2015, PREPA reviewed the SPCC plans for EPA’s Five-Year Review for Aguirre, San Juan, Palo Seco, Costa Sur, Cambalache and Mayaguez. Also, PREPA will amend the SPCC plans for the substations and Transmission and Distribution offices.

*Facility Response Plans (FRPs)*

Some facilities are also required to implement Facility Response Plans (FRP), depending on the fuel storage capacity and risk of harm to navigable waters and extent of risk they present with respect to an oil spill to a body of water. PREPA prepared and submitted the Five-Year review FRP’s for Aguirre Power Complex, San Juan Power Plant, Cambalache Turbine Gas Station, Mayaguez Gas Turbine Station and Palo Seco Power Plant to the United States Coast Guard for approval.

*Operation Manual*

Other PREPA’s facilities are required, by the federal law, to have an Operation Manual implemented for the oil transfers operations. The Operation Manuals for San Juan and Palo Seco Power Plants, Aguirre Power Complex and Cambalache and Mayaguez Turbine Gas Stations has been amended and approved by the United States Coast Guard.

*PCB Program*

The Authority completed on 2000, a tenyear EPAm mandated program to sample and test its oil filled transformers and other equipment in order to identify and dispose of PCB equipment. Pursuant to this program, the Authority has completed the removal and disposal of transformers with PCB concentrations of more than 500 ppm. The Authority continues with the removal and disposal of transformers with PCB concentrations between 50 and 499 ppm. According to EPA, the Authority has been the only utility to go so far with a program sample, test, identify, remove, and dispose of PCB or PCB contaminated transformers.
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Facilities and operations of the Authority are subject to regulation under numerous Federal and Commonwealth environmental laws, including the Clean Air Act, Clean Water Act, Oil Pollution Act (OPA), Resource Conservation Recovery Act (RCRA), Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and Underground Storage Tanks, among others.

Capital Improvement Program

The Authority's capital improvement program for fiscal year that ended June 30, 2015 includes $13.7 million in order to comply with existing Commonwealth and federal environmental laws and regulations, including the South Coast water related projects in compliance with the Clean Water Act 316(a) and 316(b) sections previously discussed. The Authority is taking all necessary steps to comply with all applicable environmental laws, regulations, and the Consent Decrees’ requirements.

Self-Insurance Health Program

Changes in the balances of the health insurance program (self-insurance risk) incurred but not recorded (IBNR) during fiscal year 2015 were as follows:

<table>
<thead>
<tr>
<th>Liability Ending Balance</th>
<th>Expense (In thousands)</th>
<th>Payments (In thousands)</th>
<th>Liability Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>$5,732</td>
<td>$64,330</td>
<td>$64,915</td>
</tr>
</tbody>
</table>

These amounts are included in accounts payable and accrued liabilities in the statement of net position.

Contingencies

General

The Authority is a defendant or codefendant in numerous legal proceedings pertaining to matters incidental to its business and typical for an electrical utility of its size and nature, including claims for damages due to electrified wires, failure to supply power and fluctuations in the power supply. Pursuant to the Act, the Authority is authorized to sue and be sued by individuals or legal entities.
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Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended (Act No. 9), the Commonwealth may provide its officers and employees, including directors, executive directors and employees of public corporations and government instrumentalities and mayors of the municipalities of the Commonwealth, with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the amount of the judgment that may be paid under the provisions of Act No. 9 in cases before federal court, but in all other cases the Secretary of Justice of the Commonwealth may determine whether, and to what extent, the Commonwealth will assume payment of such judgment. Although the Authority’s directors, executive director and employees are covered by the provisions of Act No. 9, Article 19 of Act No. 9 requires the Authority to cover the costs associated with judgments, expenses and attorneys’ fees incurred by the Commonwealth in the legal representation of its directors, executive director and employees. To the extent the Authority is unable to cover these costs and expenses, the Authority would be required to reimburse the Commonwealth from future revenues, as provided by the Secretary of the Treasury of the Commonwealth in consultation with the Authority’s board of directors. 

Abengoa Litigation 

In May 2000, Abengoa, Puerto Rico, S.E., the Authority’s original contractor for the construction of the new generating units (Units 5 and 6) at the San Juan power plant, unilaterally declared a termination of the contract and filed a complaint for breach of contract. The Authority filed a counterclaim for breach of contract and for all damages caused to the Authority by the contract termination. On September 21, 2007, the Regional Administering Judge for the Superior Court of San Juan certified the case as complex civil litigation pursuant to the Authority’s petition. On July 27, 2011, Mr. Angel F. Rossy García, a retired Commonwealth appeals court judge, was named as special master for the case. After his appointment, the special master intervened as a neutral evaluator for purposes of assisting the parties in reaching a potential settlement. The parties filed their respective position papers stating their legal contentions and case theories in August 2011. After reviewing the position papers and meeting separately with each party to discuss the strength and weakness of their respective cases, the parties were unable to reach a settlement agreement. The special master then determined that the contested issues would be resolved at trial and that the case would be bifurcated into two phases: a liability phase that would determine whether the termination was wrongful and a damages phase.
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The parties in the litigation are: Abengoa PR, SE (Plaintiff Counter defendant); PREPA (Defendant Counter plaintiff and Third-Party Plaintiff); Abengoa, SA (Third Party Defendant and Counter plaintiff); AIG (Third Party Defendant and Counter plaintiff); UNIPRO (Intervenor) and INDUTECH (Intervenor).

In order to mitigate its possible losses, the Authority entered into an agreement with Washington Engineers P.S.C. for the completion of the generating units, having said units entered into service in 2009. Expert reports have been developed assessing potential damages to be recovered from Abengoa, including excess amounts billed to the Authority prior to the wrongful termination.

This Complex Litigation was bifurcated into a liability and a damages phase. Trial on the first phase to determine the question of wrongful termination (breach of contract) commenced on January 22, 2015 and was concluded during the course of that same year. Trial on the second phase to determine the questions of damages is scheduled to commence in January 2016. The trial will be heard before designated Special Master Angel F. Rossy at the Superior Court of San Juan.

On May 2016, Abengoa filed a petition in the United States Bankruptcy Court for the State of Delaware under Chapter 15, requesting the court to stay any and all proceedings against Abengoa in the United States jurisdiction. The petition was granted by the court, and all proceeding against Abengoa were stayed until the end of October 2016.

Evidentiary hearings have been postponed until January 16, 2018, because the Special Master has his calendar occupied for the rest of the year. The parties are in the process of scheduling additional meetings to carry out various chronologies which contain stipulations by topic, this process will shorten the number of days of hearings at trial when it resumes in 2018.

Economic claims have been reserved for the second phase of trial on damages. PREPA is prepared to prove direct damages arising from the wrongful termination by Abengoa (i.e. direct costs to complete Abengoa’s scope of work, equipment refurbishment, etc.) in an amount of at least of $250 million. If recovery of indirect or consequential damages is permitted by the Court, PREPA has claimed in excess of $400 million (including claims for fuel differential costs, loss of EPA credits, etc.).
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The limit of liability under the EPC Contract is 150% of the Contract Price. This represents a range of between $276 million and $310.5 million depending on which value is considered the Contract Price at the time of termination. The Penal Sum of all Performance Bonds issued by the surety in the aggregate is approximately $190 million.

PREPA understands that is has significant probabilities of prevailing on the merits or its counterclaim for wrongful termination against Abengoa and its surety American International Insurance Company. PREPA also understands that the evidence will show that Abengoa chose to terminate the Contract with knowledge of or total disregard of the financial damage that such termination would cause PREPA and the People of Puerto Rico.

_Capeco Litigation_

In 2009, a large fire at a tank farm owned by CAPECO caused major damage to surrounding areas. The Authority stored some of its fuel at this facility. In the aftermath of the fire, numerous claims were filed against CAPECO. Some of the plaintiffs included the Authority as a defendant in these suits, alleging that the Authority failed in its duty (as the owner of fuel stored at the site) to properly monitor CAPECO’s operations in the tank farm. All cases are in the initial stages and the Authority intends to vigorously defend against these claims. On August 12, 2010, CAPECO filed for bankruptcy. As a result, thereof, all proceedings against CAPECO have been stayed.

_Consumer Billing Litigation_

In 2011, separate lawsuits were filed against the Authority by various consumers claiming damages allegedly caused by incorrect and unlawful billing and invoicing practices. Several separate lawsuits that were filed in 2011 were finally consolidated in the case of Héctor Carmona Resto, et al. v. Autoridad de Energía Eléctrica, Civil No. K AC20111265 (907). The case was also certified as a complex litigation, as requested by the Authority. The consumers are claiming damages in excess of $100 million.

The consumers requested that the case be certified as a class action. The Authority filed its Reply to the Master Lawsuit and promptly opposed to the class certification request. The case is in the discovery stage.

PREPA hired an expert witness for the case. PREPA will pursue active litigation in order to show that no class action certification is warranted, and that Plaintiffs’ claims have no merit since PREPA’s billing and invoicing is made according to the applicable laws and regulations.
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PREPA’s Expert witness rendered his report. Defendants declined the idea of retaining the services of an expert. Discovery proceedings regarding the class certification issue are being conducted.

A new Judge was assigned to the case and a Status Conference was held on December 7, 2016. As result of this conference, another status was scheduled for March 23, 2017. This conference was held as scheduled and as a result thereof a hearing for class certification was scheduled for August 16, 2017. However, on July 2, 2017, PREPA filed for bankruptcy under Title III of the “Puerto Rico Oversight, Management and Economic Stability Act” (“PROMESA”), 48 U.S.C. sec. 2101 et. seq. PREPA filed the notice of stay before the state court on July 12, 2017 and the corresponding judgement staying the case was entered on August 11, 2017.

Judgment for the Authority in the case of Santiago Ramos, et al. v. AEE, et al., USDC Civil No. 11CV01987 (JAF), has been affirmed by the federal appeals court and the case has been dismissed.

In the case of Román-Rivera, et. al. v. AEE, et al., USDC Civil No. 11-2003 (DRD), the complaint was filed on October 9, 2011 by Dario Román Rivera and 9 other plaintiffs against PREPA, the then Acting Executive Director and two former Executive Directors, and 12 members of the PREPA Governing Board. Federal jurisdiction is based upon federal question jurisdiction, and the federal statute cited is the Racketeer Influenced and Corrupt Organizations Act (RICO). The amount claimed is unspecified. On August 5, 2016, this case against the Authority was dismissed.

In the case of Ismael Marrero, et al. v. PREPA, et al., Civil No. 15CV01167 JAG, Plaintiffs filed class action against PREPA, William A. Clark, Edwin Rodriguez, César Torres, several laboratories, and oil supply companies; claiming that all defendants conspired to violate RICO, with the resulting damages to plaintiffs. According to the complaint, the defendant fuel oil suppliers provided fuel oil to PREPA which failed to meet contractual specifications or failed to comply with Environmental Protection Agency (EPA) specifications and this was noncompliant. PREPA paid the same price for this allegedly cheaper oil that it paid for compliant oil. PREPA accepted the noncompliant fuel oil in exchange for undisclosed kickbacks or commissions from unspecified defendants. Plaintiffs allege they were overcharged on their monthly electricity bills as a result of the alleged RICO conspiracy.
Collectively, defendants (including PREPA) filed 14 motions to dismiss. Plaintiffs opposed these. On September 29, 2015, the magistrate Judge issued a Report and Recommendation denying the motions to dismiss. PREPA filed its objection on October 16, 2015. The court bifurcated the case and currently the case is in its class certification discovery phase. PREPA will continue to vigorously defend this case.

Plaintiffs did not claim a specific amount of damages. If Plaintiffs were to prevail on the merits, the determination of the amount of damages to be awarded would depend on expert witness analysis.

The case of Pedro Santiago v. AEE, et al., Civil No. KPE20160618, is a consumer class action against PREPA under 32 L.P.R.A., sec. 3341, also claiming unjust enrichment, damages of up to $600 million, antitrust violations, and requesting permanent injunction. A proposed class of plaintiffs, all of whom are residential energy consumers, are challenging the fuel adjustment charge and the purchase of energy charge on various grounds, including breach of contract claims. PREPA has answered the complaint and is currently working on a motion to dismiss the case in its entirety. PREPA will vigorously defend the case and maintains that there is no cause of action against PREPA.

Vitol Inc. Litigation

In 2009, the Authority filed suit in the Commonwealth of P.R. Court of First Instance (the State Court) against Vitol, Inc. and Vitol S.A. (collectively the Vitol) seeking a declaratory judgment as to the nullity of a two fuel supply agreement due to the Vitol's failure to disclose (a) certain corruption criminal charges to which Vitol S.A. pled guilty and (b) various other investigations. The Vitol removed this suit to the U.S. District Court for the District of Puerto Rico (District Court) and presented a counterclaim alleging that the Authority owed Vitol, Inc. approximately $45 million, consisting of $28 million in fuel that was delivered to, and used by, the Authority and approximately $17 million, plus interests, costs, and attorney's fees PREPA requested remand of the case back to the State Court.

On November 28, 2012, the Authority filed a second complaint against the Vitol in State Court seeking essentially the same remedies sought in the first action but as to four other certain contracts, after discovery revealed the date on which the Vitol learned of the investigations in the corruption cases. Vitol also removed this action to the District Court. PREPA requested remand back to State Court.
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The two cases were consolidated. The Authority claims approximately $3.5 billion in the aggregate. Vitol, Inc. has resolved the claim for the $17 million in excise taxes and has stated that it will amend its counterclaim to dismiss that claim. Discovery in the case is closed. The parties have submitted motions for summary judgment against each other and the corresponding oppositions and replies thereto. The motions are pending adjudication by the court.

On March 16, 2016, the District Court granted PREPA’s requests for remand and remanded both cases to State Court. On April 8, 2016, Vitol appealed to the U.S. Court of Appeals for the First Circuit (the Court of Appeals) the order remanding the cases to State Court. The Court of Appeals affirmed the order remanding the case to State Court. Vitol requested rehearing by the full court of said ruling and the Court of Appeals denied the request for rehearing as to PREPA’s claims but left pending its ruling as to Vitol’s counterclaim due to said counterclaim having been stayed as a result of PREPA’s petition under Title III of PROMESA. Vitol once again removed the case from the State Court to the District Court but this time pursuant to the Title III provisions. PREPA has requested counsel for PREPA’s representative in PREPA’s Title III proceeding to move for remand back to the State Court.

_Asbestos Litigation_

The case of Jorge Martínez, et al. v. AEE, Civil No. K DP2005-1599, which includes fifty-four former and current employees of PREPA, was consolidated with the case of Jose Flores Sanchez v. AEE, Civil No. K DP2010-1708, a retired employee of PREPA. In both cases, plaintiffs claim that they have health problems due to PREPA’s intentional failure to comply with federal and local laws regarding handling and exposure to asbestos materials. In particular, plaintiffs claim that, during the years 1972 to 1988, PREPA failed to comply with its duty to protect the plaintiffs from asbestos exposure pursuant to the requirements of OSHA and its regulation, the Constitution of the Commonwealth of Puerto Rico and local applicable laws and regulations. Plaintiffs claim $320.96 million in damages. The Authority prevailed on appeal, and the case against the Authority has been terminated without liability to the Authority.

_Tropical Solar Farm Litigation_

On November 21, 2013, Tropical Solar Farms, LLC; New Horizon Solar, LLC; Jonas Solar Energy, LLC and Roberto Torres Torres (collectively the “Plaintiffs”) filed a 58-page suit in the Commonwealth of P.R. Court of First Instance, Ponce Section, against 29 defendants and several John Does. The complaint contains a plethora of claims against multiple defendants arising from an alleged multiplicity of sources of obligations: contractual, in tort, and in breach of fiduciary
duties and the law. It encompasses private entities, a public corporation, the Puerto Rico Electric Power Authority ("PREPA") and former public officers, among others. The complaint claims monetary compensation in excess of $705 million.

The complaint alleges that the defendants negotiated several Renewable Power Purchase Agreements to provide up to 40 megawatts to PREPA, all of which were assigned by the plaintiffs to various other defendants. In a summary, the Plaintiffs allege that the defendants never intended to comply with their obligations under the agreements, and were only buying time to advance their other renewable energy projects with PREPA.

PREPA filed a motion to dismiss and on October 2, 2015 a partial judgment was entered dismissing all claims in the case against PREPA with prejudice.

Tropical Solar has appealed the dismissal to the Puerto Rico Court of Appeals. The Puerto Rico Court of Appeals modified the dismissal of the claims against PREPA from a dismissal with prejudice to a dismissal without prejudice. The claims remain dismissed without prejudice.

**KDC Solar PRSI, LLC Arbitration**

On December 13, 2011, PREPA and Ciro Energy Corp. (Ciro) entered into a Master Renewable Power Purchase and Operating Agreement (the MPPOA) pursuant to which Ciro, in its discretion, could propose PREPA solar photovoltaic energy projects of up to 20 MWs each an up to 100 MWs in the aggregate, and pursuant to which, if PREPA’s system could interconnect the proposed projects, and PREPA accepted a proposed site and interconnection point, PREPA and Ciro could enter into a Power Purchase and Operating Agreement (PPOA) for each proposed and accepted project.

On December 11, 2012, Ciro assigned the MPPOA to KDC Solar PRC LLC (PRC), subject to PREPA consenting to the assignment and effective on the date of PREPA’s consent to the assignment. On January 9, 2013, PREPA consented to the assignment of the MPPOA by Ciro to PRC.

On February 26, 2015, KDC Solar PRSI LLC (PRSI) filed a demand for arbitration against PREPA, which was later amended on December 18, 2015. In the amended demand for arbitration, PRSI claims that PREPA had an obligation to award PPOAs to PRSI and that PREPA breached its obligations under the MPPOA by refusing award PPOAs to PRSI under the MPPOA. PRC has requested to be substituted as claimant in the arbitration.
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PRSI claims damages in an amount between $43.9 and $51.9 million. PREPA has denied any liability to PRSI or PRC and has asserted that PREPA did not have an obligation to award a PPOA to PRSI or PRC under the MPPOA because the same is not a contract, and that, to the extent that the MPPCA is a contract, the same is null and void for lack of consideration and due to the parties’ failure to provide PREPA the sworn statement required by ACT 458 of 2000, as amended, among other defenses raised by PREPA in its answer to the amended demand for arbitration.

The Puerto Rico Court of Appeals modified the dismissal of the claims against PREPA from a dismissal with prejudice to a dismissal without prejudice. The claims remain dismissed without prejudice.

*Tradewinds Energy Barceloneta LLC and Tradewinds Energy Vega Baja Arbitration*

PREPA and Tradewinds Energy LLC entered into two Power Purchase and Operating Agreements (PPOAs) to develop aeolic (wind) energy facilities, which were assigned to Tradewinds Energy Barceloneta and Tradewinds Energy Vega Baja (collectively Tradewinds). On January 18, 2016, Tradewinds filed a demand for arbitration under the two PPOAs claiming $30 million in damages. The parties have already selected the arbitrator, but have yet to execute the arbitration submission agreement so that the Authority may proceed to answer the demand for arbitration. PREPA will deny any and all liability to Tradewinds and denies having breached any obligations under the PPOAs. The case has been stayed as a result of the filing of PREPA’s Title III petition.

*Resun (Barceloneta) LLC Litigation and Arbitration*

Resun (Barceloneta) LLC (Resun) and PREPA entered into a Power Purchase and Operating Agreement (PPOA). Resun claims that PREPA breached its obligations under the PPOA and demanded arbitration. PREPA asserted that it did not have to submit to arbitration yet and Resun filed a complaint before the State Court to compel PREPA to submit to arbitration. PREPA filed a motion for summary judgment to dismiss the complaint to compel and the State Court granted PREPA’s motion and dismissed the complaint to compel arbitration. Resun appealed the judgment of dismissal. PREPA filed its appellee brief. The Court of Appeals affirmed the summary judgement of dismissal. Resun filed a petition for certiorari before the PR Supreme Court, which was stayed as a result of the filing of PREPA’s Title III petition.
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While ReSun has not asserted anywhere the amount of damages that it alleges is has suffered as a result of PREPA’s alleged breach of its obligations under the PPOA, PREPA anticipates that once an amount is asserted it may be in excess of $10 million.

Passco, Inc. Litigation

PREPA and Passco entered into a contract for the design, delivery manufacture, installation, calibration, testing and successful startup of a New Battery Bank for each Power Converter System of the Sabana Llana Battery Energy Storage System (BESS). Passco subcontracted Nife Baterias Industrias (a Brazilian company), for the design and manufacture of the BESS. Due to serious flaws in the design, construction and installation of the BESS, a fire occurred and caused extensive damages to the BESS, which is inoperative and unusable.

On May 24, 2007, PREPA filed a suit in the Commonwealth of P.R. Court of First Instance, San Juan Section, against Passco, Nife, the surety (Compañía de Fianzas de Puerto Rico or “CFPR”) and the insurer (AIG). PREPA claims breach of contract and damages in excess of $19 million.

Sometime in 2007, Nife filed for bankruptcy in Brazil. The surety, CFPR, is in a liquidation process and the Insurance Commissioner is acting as the liquidator. On March 19, 2015, Passco filed for bankruptcy in Puerto Rico.

AIG filed motions for summary judgment under the CGL and COPS policies it issued to PREPA, arguing that the policies issued by AIG exclude coverage for the damages sought by PREPA. PREPA timely filed its oppositions to AIG’s motions for summary judgment. AIG’s motion for summary judgment was denied. AIG filed a petition for certiorari of said denial and the PR Court of Appeals denied the petition for certiorari. AIG filed a motion for reconsideration of said denial and PREPA opposed the same. The PR Court of Appeals denied AIG’s motion for consideration. The case is in the discovery phase. PREPA settled its claim against the CFPR.

Real Legacy Assurance Co. Litigation

On December 29, 2006, an electric arc occurred and caused an ensuing fire in PREPA’s Pelo Seco Plant in Cataño, Puerto Rico, and caused damages to generating unit #1 (Unit 1). On October 6, 2010, PREPA filed a complaint against Real Legacy Assurance Co. (RLA) requesting $3,682,836 in physical damages and $22,560,257 in extra expenses. RLA filed a motion for
summary judgment arguing that RLA’s insurance policy excludes coverage for the electrical damages and extra expense claimed by PREPA. PREPA timely filed its opposition. The Court denied RLA’s motion. On August 14, 2017, the Authority and RLA signed a transactional agreement and the case was dismissed on November 16, 2017.

**PBJL Energy Corporation Litigation**

On December 20, 2011, PREPA and PBJL Energy Corporation (PBJL) entered into a Master Renewable Power Purchase and Operating Agreement (MPPOA) pursuant to which PBJL, in its discretion, could propose to PREPA solar photovoltaic energy projects of up to 20MWs each and up to 100 MWs in the aggregate, and pursuant to which, if PREPA’s system could interconnect the proposed projects, and PREPA accepted a proposed site and interconnection point, PREPA and PBJL could enter into a Power Purchase and Operating Agreement (PPOA) for each proposed and accepted project.

On May 5, 2015, PBJL filed a complaint against PREPA and various PREPA employees in their official and personal capacity, claiming that PREPA had an obligation to award PPOAs to PBJL and that PREPA breached its obligations under the MPPOA by refusing to award PPOAs to PBJL under de MPPOA.

PBJL claims damages in the amount of $210,985,000. PREPA has denied any liability to PBJL and has asserted that PREPA did not have the obligation to award a PPOA to PBJL under the MPPOA because the same is not a contract, and that, to the extent that the MPPOA is a contract, the same is null and void for lack of consideration and due to PBJL’s failure to provide PREPA the sworn statement required by Act 458 of 2000, as amended, among other defenses raised by PREPA in its answer to the complaint.

PREPA filed a motion to dismiss the complaint against the PREPA employees, which the Court granted.

The case is currently in the stage of discovery proceedings.

**CMA Builders**

This is a cash collection action related to a bid bond furnished with the proposal forfeited in favor of PREPA. It was furnished after CMA was awarded the auction for supplying fuel oil but later failed to enter into a Contract with PREPA. The case was referred to the law firm of Cancio,
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Nadal, Rivera & Díaz and thereafter a motion to a reconsider was filed before the Puerto Rico Court of Appeals. This was denied by said Appellate Court on May, 19, 2017. On June 26, 2017, PREPA filed a Certiorari before the Supreme Court of Puerto Rico.

*Samuel Rodríguez Claudio, et al. v. AEE*

This is an action for damages suffered, filed by a person who got electrocuted by a PREPA cable while working on the roof of a business on Guavate. He sustained damages to his body. The complaint was filed on July 2013 claiming damages amounting to $4 million. Currently in discovery, third-party complaint filed by PREPA against contractor and inspector working the site. The case was in discovery and PREPA filed a third party complaint against the contractor and the inspector working the site. However, on July 2, 2017, PREPA filed for bankruptcy under Title III of the “Puerto Rico Oversight, Management and Economic Stability Act” (“PROMESA”), 48 U.S.C. sec. 2101 et. seq. PREPA filed the notice of stay before the state court on July 13, 2017.

*Juan Carlos Pérez Irene, Et. Al v. Autoridad de Energía Eléctrica, Et Al.*

This is an action for damages suffered filed by several persons (one of them deceased) and the members of their respective families when, upon attempting to work on air conditioning units on the roof of a certain building, they received electric shocks from a high voltage wire nearby. One of them was electrocuted. Plaintiffs claim damages in excess of Two Million Dollars. The judge granted PREPA’s motion to bifurcate the issues of liability and damages. PREPA filed a dispositive motion as to liability since its position is that it is the building’s owner who is liable, as his structural changes to the original building brought the roof in close proximity to the high-tension wire, in violation of PREPA’s easements. This was opposed by plaintiff, who also filed a motion for summary judgment. PREPA opposed the same. The Court did not rule on any of these dispositive motions. Trial as to liability was held on August 2016 and judgment dismissing the action against PREPA was entered on April 18, 2017. Plaintiffs have appealed the judgment before the Puerto Rico Court of Appeals, which appeal is pending. PREPA will continue to vigorously defend this case.

However, on July 2, 2017, PREPA filed for bankruptcy under Title III of the “Puerto Rico Oversight, Management and Economic Stability Act” (“PROMESA”), 48 U.S.C. sec. 2101 et. seq. PREPA filed the notice of stay before the Appeals Court on July 11, 2017.
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_Rafael González Reyes; Omayra Ocasio v. Autoridad de Energía Eléctrica_  

This is a complaint for damages allegedly caused by Mr. González Reyes’ contact with an electrical cable while trying to get some fruit from a tree. There is no death involved, but there were extensive burns to his body. Plaintiffs claim $1,880,000 for damages. The complaint was answered denying any liability on behalf of PREPA. Plaintiff has been deposed and been medically evaluated, which evaluation has concluded that plaintiff Mr. González has a 51% whole body impairment as a consequence of this contact. Therefore, the damages suffered in this case by plaintiff can be characterized as catastrophic. A Status Conference was held on June 6, 2017. On July 2, 2017, PREPA filed for bankruptcy under Title III of the “Puerto Rico Oversight, Management and Economic Stability Act” (“PROMESA”), 48 U.S.C. sec. 2101 et. seq. PREPA filed the notice of stay before the State Court on July 11, 2017 and judgment was entered according on July 31, 2017.  

_Patricia Guevara Bariska_  

On April 27, 2013 Jose M Guevara was engaged in a certain construction work at the premises of IFCO Recycling Company located in Caguas. At about 2:00PM Guevara lifted a tool (known as “bull float” a type of rake that is used for leveling concrete) that was on the ground, suddenly an explosion was heard when an electricity arc was released from one of PREPA’S high voltage electricity line that was too low. Mr. Guevara was electrocuted and died. Plaintiffs claim emotional and mental damages for their loss, compensatory, not punitive.  

On February 6, 2014, the complaint was filed in the US District Court, District of Puerto Rico.  

The theory asserted by plaintiff establishes that Electric lines height did not comply with PREPA regulations and applicable laws. PREPA’s negligence, breach and lack of care in this case was the catalytic agent that caused the fatal incident to which this case refers.  

The parties have exchanged settlement proposals, plaintiffs asked for $2 million and PREPA offered $200,000. The case was scheduled for trial, however on July 2, 2017, PREPA filed for bankruptcy under Title III of the “Puerto Rico Oversight, Management and Economic Stability Act” (“PROMESA”), 48 U.S.C. sec. 2101 et. seq. PREPA filed the notice of stay before the state court on July 13, 2017.  

On July 10, 2017 the United States District Court for the District of PR stayed this case due to the Chapter III filing under PROMESA by PREPA.
Emmanuel A. Estrada Lopez v. PREPA

On July 15, 2015, Emanuel Estrada filed a suit in relation to PREPA. Mr. Jan Alejandro Estrada (Emanuel’s Father), while working in the backyard of a private home, came in contact with an energized wire in the yard and died by electrocution.

It is the plaintiff’s contention that the line became energized due to PREPA negligence. The Plaintiff is claiming damages for pain and suffering in an amount of $3,000,000.00, plus payment of costs and attorney’s fees.

At this point in time, the complaint has been answered, denying any act or negligent omission on the part of PREPA. The parties exchanged discovery, and took all depositions excluding those of the experts. PREPA was found to have destroyed evidence (spoliation) and consequently sanctioned. The spoliation issue was appealed. PREPA filed a Petition for Certiorari before the Puerto Rico Appellate Court, which is now pending.

Pretrial was scheduled for August 25, 2017 and trial for October 30, 2017 to November 30, 2017.

On July 2, 2017, PREPA filed for bankruptcy under Title III of the “Puerto Rico Oversight, Management and Economic Stability Act” (“PROMESA”), 48 USC sec. 2101 et seq. PREPA filed a Notice of Stay before the trial Court on June 12, 2017 and the one before the Appellate Court on July 11, 2017. PREPA has and will continue to vigorously argue and defend this case. At this stage of the proceedings there is cause for concern regarding the high possibility of a finding of negligence against PREPA. The facts indicate that a ceramic isolator was rusted and broken, and as a result, it fell on the guy wire and energized it, causing decedent’s death.

Tec General Contractors v. PREPA

On July 1, 2015 Tec General Contractors filed a suit due to Breach of contract regarding the Rehabilitation of the Guajataca Canal Project. PREPA contracted CSA for the preparation of blueprints and project specifications. Once received, PREPA celebrated the bidding process. The project was finally awarded to Tec General Contractors. After works began, PREPA contracted with CSA once again for inspection services during the project. During the project, both PREPA and CSA requested changes to the original project specifications which resulted in material changes to the project and additional costs to Tec General.
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After merits trial, judgment was entered against PREPA and CSA jointly for $1,273,619. PREPA was also found liable for administrative expenses and retainer fee for a total of $173,847. The case was appealed by both PREPA and CSA. On July 19, 2017 PREPA filed Notice of Stay, having filed for bankruptcy under PROMESA on July 2, 2017. The case is currently stayed. Plaintiffs moved for reconsideration for stay as to CSA to be lifted. Both PREPA and CSA have opposed the petition for reconsideration. PREPA will continue to vigorously argue and defend this action. It is reasonably probable that PREPA will not prevail.

17. Recently Issued Accounting Pronouncements

- GASB Statement No. 74, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans (GASB Statement No. 74), which is effective for fiscal years beginning after June 15, 2016. GASB Statement No. 74 establishes financial reporting standards for state and local governmental other postemployment benefit (OPEB) plans. The scope of this statement includes defined benefit and defined contribution OPEB plans administered through trusts that meet specified criteria. The Statement replaces GASB Statements No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended, and GASB Statement No. 57, OPEB Measurements by Agent Employers and Agent MultipleEmployer Plans.

- GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (GASB Statement No. 75), which is effective for fiscal years beginning after June 15, 2017. GASB Statement No. 75 addresses accounting and financial reporting for OPEB that is provided to the employees of state and local governmental employers. This Statement also establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB plans this statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosures and required supplementary information are also addressed by the statement. This statement replaces the requirements of GASB Statements No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, as amended, and GASB Statement No. 57, OPEB Measurements by Agent Employers and Agent Multiple Employer Plans, for OPEB.
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- GASB Statement No. 76, The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments (GASB Statement No. 76), which is effective for reporting periods beginning after June 15, 2015. GASB Statement No. 76 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. This statement supersedes GASB Statement No. 55, The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments. It also amends GASB Statement No. 62, Codification of accounting and financial Reporting Guidance Contained in PreNovember 30, 1989 FASB and AICPA Pronouncements, paragraph 64, 74, and 82.

- GASB Statement No. 80, Blending Requirements for Certain Component Units an Amendment of GASB Statement No. 14 (GASB Statement No. 80), which is effective for periods beginning after June 15, 2016. GASB Statement No. 80 improves financial reporting by clarifying the financial statement presentation requirements for certain component units. This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments established in paragraph 53 of GASB Statement No. 14, The Financial Reporting Entity, as amended. The additional criterion requires blending of a component unit incorporated as a notforprofit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of GASB Statement No. 39, Determining Whether Certain Organizations Are Component Units.

- GASB Statement No. 82, Pension Issues- an Amendment of GASB Statements No 67, No. 68, and No. 73, (GASB Statement No. 82), which is effective for periods beginning after June 15, 2016, except for the requirements of this Statement for the selection of assumptions in a circumstance in which an employer’s pension liability is measured as of a date other than the employer’s most recent fiscal yearend. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. GASB Statement No. 82 addresses certain issues that have been raised with respect to GASB Statements No. 67, No. 68, and No. 73. The Statement is designed to improve consistency in the application of
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the pension standards by clarifying or amending related areas of existing guidance. Specifically, this Statement addresses issues regarding (1) the presentation of payroll related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard.

- GASB Statement No. 83, Certain Asset Retirement Obligations. This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement. This Statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for AROs. This Statement requires that recognition occur when the liability is both incurred and reasonably estimable. The determination of when the liability is incurred should be based on the occurrence of external laws, regulations, contracts, or court judgments, together with the occurrence of an internal event that obligates a government to perform asset retirement activities. Laws and regulations may require governments to take specific actions to retire certain tangible capital assets at the end of the useful lives of those capital assets, such as decommissioning nuclear reactors and dismantling and removing sewage treatment plants. Other obligations to retire tangible capital assets may arise from contracts or court judgments. Internal obligating events include the occurrence of contamination, placing into operation a tangible capital asset that is required to be retired, abandoning a tangible capital asset before it is placed into operation, or acquiring a tangible capital asset that has an existing ARO.

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

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

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

- GASB Statement No. 84, Fiduciary Activities. The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. Governments with activities meeting the criteria should present a statement of fiduciary net position and a statement of changes in fiduciary net position. An exception to that requirement is provided for a business-type activity that normally expects to hold custodial assets for three months or less. This Statement describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria. This Statement also provides for recognition of a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018. Earlier application is encouraged. This statement is not expected to have material impact on the Authority’s financial statements.

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

- Blending a component unit in circumstances in which the primary government is a business-type activity that reports in a single column for financial statement presentation.
- Reporting amounts previously reported as goodwill and “negative” goodwill.
- Classifying real estate held by insurance entities.
- Measuring certain money market investments and participating interest earning investment contracts at amortized cost.
- Timing of the measurement of pension or OPEB liabilities and expenditures recognized in financial statements prepared using the current financial resources measurement focus.
- Recognizing on-behalf payments for pensions or OPEB in employer financial statements.
- Presenting payroll-related measures in required supplementary information for purposes of reporting by OPEB plans and employers that provide OPEB.
- Classifying employer-paid member contributions for OPEB.
- Simplifying certain aspects of the alternative measurement method for OPEB.
- Accounting and financial reporting for OPEB provided through certain multiple-employer defined benefit OPEB plans.

The requirements of this Statement are effective for reporting periods beginning after June 15, 2017. Earlier application is encouraged.

- GASB Statement No. 86, Certain Debt Extinguishment Issues. This Statement improves the consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. The requirements of this Statement are effective for fiscal years beginning after June 15, 2017. Earlier application is encouraged.
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- GASB Statement No. 87, Leases. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments’ financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments’ leasing activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2019. Earlier application is encouraged.

Management is evaluating the impact that these Statements will have on the Authority’s basic financial statements.

18. Adoption of GASB 68 and Prior Period Adjustment

GASB 68, Accounting and Financial Reporting for Pensions, became effective on July 1, 2014, which was amended by and GASB 71, Pension Transition for Contributions Made Subsequent to the Measurement Date, requires measurement and recognition of net pension liability, deferred outflows and inflows of resources and expenses related to the government sponsored plan. As a result of the implementation of GASB 68 and GASB 71, the Authority recognized a $1,644 million prior period adjustment on beginning net position as of July 1, 2014.

The impact on the Authority net position is as follows:

<table>
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<tr>
<th></th>
<th>Net Pension Liability</th>
<th>Deferred outflow of resources</th>
<th>Net Investment in capital assets</th>
<th>Unrestricted</th>
<th>Total</th>
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<td>As originally reported</td>
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<td>$ (253,448)</td>
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<td>$ (1,267,005)</td>
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19. Financial Condition and Liquidity  

The Authority has defaulted on various debt obligations and does not currently have sufficient funds available to fully repay its various obligations as they come due. Commencing in August 2014, the Authority executed forbearance agreements and, ultimately in November 2015, a restructuring support agreement with its major creditors account to which they agreed to refrain from exercising contractual remedies in relation to such obligations. The Authority worked with such creditors on implementing a restructuring and recovery plan based on extending the due date of its obligations and obtaining other creditor concessions, including reducing the principal amount of certain of its debts, obtaining more favorable covenants and other terms under the Trust Agreement securing its outstanding power revenue and revenue refunding bonds (the "Bonds" and the "Trust Agreement") and obtaining new financing to repay other outstanding obligations, while continuing to operate and to finance capital improvement projects. This plan was rejected by the Financial Oversight Board of Puerto Rico and the Authority has commenced proceedings under Title III of PROMESA.

The Commonwealth and its instrumentalities are also experiencing significant financial difficulties and may be unable to continue to repay amounts due to the Authority or extend, refinance or otherwise provide the necessary liquidity to the Authority as and when needed. Additionally, the overall economy in Puerto Rico has declined. These difficulties were worsened by the recent hurricane damage, including to infrastructure, such as the Authority's facilities, as described more fully in Note 20, Subsequent Events, below. The Authority has receivables of over $1,707 million payable by the Commonwealth and related entities and is subject to significant uncertainty with regard to its ability to collect on such receivables. As a result, at June 30, 2015, the Authority has reserved $83 million for uncollectability based on subsequent collections. During the year ended June 30, 2015, the Authority has also recognized a $146.7 million impairment on deposits held at GDB.

The Authority may not be able to avoid further defaults on its obligations. Management plans to address the Authority's liquidity situation and continue providing services through the Title III process as described below. There can be no assurance, however, that: (i) the Authority will be able to refinance or modify the terms of its obligations; (ii) management's plan will provide for the ability to repay or refinance the obligations or extend their terms; or (iii) certain services will not have to be modified, curtailed or terminated.
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20. Subsequent Events  

Provisional Rate  

On May 27, 2016, the Authority filed a petition before the Energy Commission seeking approval of an adjustment to the rates charged to the Authority’s customers. The petition sought approval of the proposed rate adjustment on a temporary basis pending the Energy Commission’s consideration of the requested rate adjustment. On June 24, 2016, the Energy Commission issued an order authorizing the Authority to increase its rates, on a temporary basis, by approximately 1.3 cents per kWh, effective as of thirty days after issuance of the order, subject to certain conditions. The rate adjustment generated additional revenues for the fiscal year ended June 30, 2017 of approximately $220 million.  

On January 10, 2017, the Energy Commission issued a Final Resolution and Order lowering the revenue requirement to $177 million, which resulted in an average rate increase of approximately 1.025 cents per kWh. However, on January 20, 2017, the Authority filed its Motion for Clarification regarding, among other things, the base revenue requirement calculation. In response, on March 8, 2017, the Commission issue a Resolution in response that approved a revised revenue requirement increase of $171.786 million. Therefore, on April 25, 2017, the Authority filed its Compliance Filing basing rates on the updated revenue requirement calculation, which was approved, subject to certain modifications, in May 10, 2017 and May 31, 2017 Orders. The Authority is required to provide a credit on customer bills for the difference between the provisional rate revenues and the final approved rate, in accordance with these Orders and the requirements of Act 83, as amended by Act 4-2016.  

Due to Hurricane María, the Energy Commission temporarily suspended, effective September 19, 2017, all administrative proceedings including the provisional and final rate implementation issues. On November 1, 2017, in the rate case docket, the Energy Commission granted, in part, and denied, in part, the Authority’s motion to postpone the permanent rate implementation. Specifically, the Energy Commission granted the Authority’s request for temporary extension of the provisional rate and of all other deadlines, under the rate order and subsequent orders, regarding permanent rate implementation and the provision of information regarding reconciliations and budgetary oversight and approvals, under Section 6A of Act 83-1941 and Article 6.25 of Act 57-2014. The Energy Commission also ordered that it would issue a new timeline for compliance and filing deadlines when the Authority’s operations are normalized.
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**Integrated Resources Plan (IRP)**

In July 2015, the Authority submitted a proposed integrated resources plan (as amended, the “IRP”) to the Energy Commission, as required under the Puerto Rico Energy Transformation and Relief Act (Act No. 57-2014). On September 23, 2016, following multiple hearings, the Energy Commission approved a modified IRP including key elements of the Authority’s proposed IRP to upgrade the Authority’s transmission, distribution and generation systems. The modified IRP expressly did not include approval of the construction of the Aguirre Offshore Gas Port (“AOGP”) and related conversion projects, as proposed by the Authority. However, it does allow the Authority to continue the relevant permitting process for AOOGP and Authority expenditures for the project up to a cap of $15 million. The Authority filed a motion for reconsideration and clarification on October 10, 2016, which the Energy Commission granted, in part, and denied, in part on February 10, 2017. Also, on February 10, 2017, the Commission opened a separate but related new docket entitled “Aguirre Site Economic Analysis,” to obtain further information about the merits and viability of AOOGP and the conversions, and of potential alternatives. The Authority supplied the required information for its proposal. The Aguirre case is pending a final Energy Commission decision. There is no deadline for the final order. Although the submission of the next IRP would otherwise be due in 2018, several compliance items remain open from the last IRP. In a November 1, 2017 order in Case No. CEPR-AP-2015-0002 (the IRP docket), the Commission extended until December 31, 2017 “all pending compliance filing due dates” in the IRP proceeding.

**Key Legislation Prior to PROMESA**

**Act 57-2014**

On May 27, 2014, the Commonwealth of Puerto Rico enacted Act No. 57 of 2014 (“Act 57-2014”), also known as the *Transformation and Energy Relief Act of Puerto Rico*. Act 57-2014 provides for, among other things, the creation of the Puerto Rico Energy Commission with regulatory oversight over the Authority’s operations, as well as over any other company providing electric energy services in Puerto Rico. The Energy Commission has since been formed, has evaluated plans that the Authority is required to submit to the Energy Commission and has reviewed and approved the electric rates proposed by the Authority.
Act 4-2016: The PREPA Revitalization Act

On November 4, 2015, the Governor submitted the PREPA Revitalization Act to the Legislative Assembly to facilitate the Authority’s ongoing transformation and recovery plan. The PREPA Revitalization Act set forth a framework for the Authority to execute on the agreements with creditors reached to that date. Among other things, the PREPA Revitalization Act would (1) enhance the Authority’s governance processes; (2) adjust the Authority’s practices for hiring and managing personnel; (3) change the Authority’s processes for collecting outstanding bills from public and private entities; (4) improve the transparency of the Authority’s billing practices; (5) implement a competitive bidding process for soliciting third-party investment in the Authority’s infrastructure; (6) allow for the refinancing of existing Authority bonds through a securitization that would reduce the Authority’s indebtedness and cost of borrowing; and (7) set forth a process for the Energy Commission to address the Authority’s proposal for a new rate structure that is consistent with its recovery plan. The PREPA Revitalization Act was approved by the Senate of Puerto Rico on February 10, 2016 and by the House of Representatives, with amendments, on February 15, 2016. The Senate concurred with these amendments and the Governor signed Act 4-2016 into law on February 16, 2016. In light of the termination of the RSA and the commencement of the Title III case for the Authority (as discussed below), the securitization transactions contemplated by the PREPA Revitalization Act have not occurred.

The PREPA Revitalization Act authorized the Puerto Rico Electric Power Authority Revitalization Corporation ("PREPARC") to issue securitization bonds and impose a transition charge on the Authority’s customers, with an automatic adjustment mechanism, for the purpose of allowing the Authority to restructure certain of its financial indebtedness as contemplated by the RSA. On April 7, 2016, PREPARC filed a petition before the Energy Commission seeking approval of the calculation methodology for the transition charge and the related adjustment mechanism. On June 21, 2016, the Energy Commission approved PREPARC’s petition, and on June 28, 2016, PREPARC approved a resolution authorizing the issuance of the new securitization bonds, subject to certain terms and conditions. In light of the termination of the RSA and the commencement of the Title III case for the Authority (as discussed below), the securitization transactions contemplated by the PREPA Revitalization Act have not occurred.

On August 7, 2017, the Puerto Rico Senate introduced Senate Bill 608, which proposes to eliminate PREPARC. As of December 2017, no action has been taken on Senate Bill 608.
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**Act 21-2016: The Moratorium Act**

On April 6, 2016, then-Governor García Padilla signed into law the Moratorium Act. Among other objectives, the Moratorium Act allowed the Governor to declare a moratorium on debt service payments and to stay related creditor remedies against the Commonwealth and its component units for a temporary period. The initial temporary period set forth in the Moratorium Act was set to expire on January 31, 2017, with a possible two-month extension at the Governor’s discretion. The moratorium and stay provisions of the Moratorium Act required executive action of the Governor to become effective.

The Moratorium Act also included amendments to GDB’s organic act to include certain statutory options and tools useful for any resolution, reorganization or restructuring that GDB may undertake in the future. Specifically, these amendments modernized the receivership provisions in the GDB’s organic act and authorized the creation of a temporary “bridge bank” to carry out the GDB’s functions and honor deposits.

The Moratorium Act also created a new Commonwealth government agency—the Fiscal Agency and Financial Advisory Authority (“AAFAF” by its Spanish acronym)—to assume GDB’s role as fiscal agent, financial advisor and reporting agent for the Commonwealth, its instrumentalities, and municipalities.

Pursuant to the Moratorium Act, on April 8, 2016, the Governor issued executive order OE-2016-010, declaring GDB to be in a state of emergency. In accordance with the emergency powers provided in the Moratorium Act, OE-2016-010 implemented a regulatory framework governing GDB’s operations and liquidity, including prohibiting loan disbursements by GDB and establishing a procedure with respect to governmental withdrawals, payments, and transfer requests in respect of funds held on deposit at GDB. To that effect, OE-2016-010 restricted the withdrawal, payment and transfer of funds held on deposit at GDB to those reasonable and necessary to ensure the provision of essential services and authorized GDB to establish weekly limits on the aggregate amount of such disbursements.

The procedures implemented by OE-2016-010 resulted in restrictions on the ability of the Commonwealth and its component units to withdraw funds held on deposit at GDB. On April 1, 2016, the Commonwealth began depositing its revenues in accounts outside of GDB. However, the Puerto Rico Treasury Department still has funds deposited at GDB, subject to the limitations on withdrawals of funds from GDB. The executive order resulted in restriction on the ability of the Authority to withdraw any funds held on deposit at GDB.
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As of December 31, 2017, the Authority had $144.7 million deposited at GDB, which were reserved for uncollectibility.

On April 30, 2016, the Governor issued executive order OE-2016-014, which declared a payment moratorium with respect to certain obligations of GDB. Pursuant to OE-2016-014, GDB failed to make a principal payment of approximately $367 million in respect of its notes on May 1, 2016.

On June 30, 2016 (the same day as the enactment of PROMESA), the Governor issued executive order OE-2016-030, declaring the Commonwealth to be in a state of emergency and declaring a moratorium on the Commonwealth’s obligation to make payments on bonds and notes issued or guaranteed by the Commonwealth. On the same date, the Governor also issued executive order OE-2016-031, which, among other things, declared an emergency period with respect to certain Commonwealth instrumentalities, including the Puerto Rico Convention Center District Authority (“PRCCDA”), the Employees’ Retirement System (“ERS”), the Puerto Rico Industrial Development Company (“PRIDCO”), the University of Puerto Rico (“UPR”), and the Puerto Rico Public Finance Corporation (“PFC”).

As a result of the enactment of the Moratorium Act and the subsequent executive orders described above, on October 18, 2016, the Secretary of the Treasury issued Circular Letter No. 1300-08-17 (“CC 1300-08-17”) alerting the Commonwealth’s agencies and component units with funds deposited with GDB that such deposits were exposed to credit risk as a result of GDB’s liquidity shortage and corresponding insolvency situation. CC 1300-08-17 also reminded the Commonwealth’s agencies and component units that, in light of the Moratorium Act and OE-2016-010, GDB believed there was substantial doubt about its ability to continue as a going concern. For all these reasons, CC 1300-08-17 urged all Commonwealth agencies and component units with funds deposited with GDB to conduct an impairment analysis on such deposits as of June 30, 2015 and June 30, 2016.

**PROMESA**

On June 30, 2016, President Barack Obama signed into law the *Puerto Rico Oversight, Management, and Economic Stability Act*, codified under 48 U.S.C. §§ 2101-2241 (“PROMESA”). In general terms, PROMESA seeks to provide the Commonwealth with fiscal and economic discipline through, among other things: (i) the establishment of the Oversight Board, whose responsibilities include the certification of fiscal plans and budgets for the Commonwealth and its related entities; (ii) a temporary stay of all creditor lawsuits; and (iii) two alternative methods to adjust unsustainable debt: (a) a voluntary debt modification process under
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Title VI of PROMESA, which establishes a largely out-of-court debt restructuring process through which modifications to financial debt can be accepted by a supermajority of creditors; and (b) a quasi-bankruptcy proceeding under Title III of PROMESA, which establishes an in-court debt restructuring process substantially based upon incorporated provisions of the U.S. Bankruptcy Code (11 U.S.C. §§ 101, et seq.). Each of these elements are divided among PROMESA’s seven titles, as discussed below.

(i)  Title I — Establishment of Oversight Board and Administrative Matters

Upon PROMESA’s enactment, the Oversight Board was established for Puerto Rico. See PROMESA § 101(b). As stated in PROMESA, “the purpose of the Oversight Board is to provide a method for a covered territory to achieve fiscal responsibility and access to the capital markets.” PROMESA § 101(a). On August 31, 2016, President Obama announced the appointment the Oversight Board members. Each Oversight Board member is required to have “knowledge and expertise in finance, municipal bond markets, management, law, or the organization or operation of business or government.” PROMESA § 101(f)(1). The Oversight Board was “created as an entity within the territorial government for which it [was] established” and is expressly not an entity of the federal government, see PROMESA § 101(c), but it was also established to act independently from the Commonwealth government, such that neither the Governor nor the Legislative Assembly may “(i) exercise any control, supervision, oversight, or review over the Oversight Board or its activities; or (ii) enact, implement, or enforce any statute, resolution, policy, or rule that would impair or defeat the purposes of [PROMESA], as determined by the Oversight Board.” PROMESA § 108(a). Please refer to the language of PROMESA for a complete description of the Oversight Board and its powers.

(ii)  Title II — Fiscal Plan and Budget Certification Process and Compliance

Title II sets forth the requirements for proposing and certifying fiscal plans and budgets for the Commonwealth and its instrumentalities. “Each fiscal plan serves as the cornerstone for structural reforms the Oversight Board deems necessary to ensure the territory, or instrumentality, will be on a path towards fiscal responsibility and access to capital markets.” H.R. Rep. 114-602(I), 2016 WL 3124840, at *45 (2016); PROMESA § 201(b)(1). According to the legislative history, a fiscal plan should “provide for a sustainable level of debt, improve governance, provide for capital expenditures that promise economic growth, and respect the relative priorities that different classes of bondholders have vis-à-vis one another under Puerto Rico law.” H.R. Rep. 114-602(I), 2016 WL 3124840, at *112 (2016). PROMESA section 201 sets forth the specific requirements for a fiscal plan and the process for fiscal plan approval.
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Only after the Oversight Board has certified a fiscal plan may the Governor submit a fiscal year Commonwealth budget and fiscal year budgets for certain Commonwealth instrumentalities (as determined by the Oversight Board) to the Legislative Assembly. See PROMESA § 201(c)(1). PROMESA section 202 sets for the specific procedures and requirements for approval of each fiscal year Commonwealth budget and Commonwealth instrumentality budgets.  

In furtherance of the foregoing duties, PROMESA contains a provision that grants the Oversight Board powers to monitor compliance with certified fiscal plans and budgets and undertake certain actions, including spending reductions and the submission of recommended actions to the Governor that promote budgetary compliance. Please refer to the language of PROMESA for a complete description of the Oversight Board’s powers related to fiscal plan and budgetary compliance.  

(iii) Title III — In-Court Restructuring Process  

Title III of PROMESA establishes an in-court process for restructuring the debts of Puerto Rico and other United States territories that is modeled after the process under Chapter 9 of the U.S. Bankruptcy Code. In order to be a debtor under Title III, the territory and/or its instrumentalities must: (i) have an Oversight Board established for it or be designated a “covered entity”; (ii) have the Oversight Board issue a restructuring certification under PROMESA section 206(b); and (iii) “desire to effect a plan to adjust its debt.” PROMESA § 302. The Oversight Board has sole authority to file a voluntary petition seeking protection under Title III of PROMESA. See PROMESA § 304(a) In May 2017, the Oversight Board approved and certified Title III filings for the Commonwealth, Puerto Rico Sales Tax Financing Corporation (COFINA), Puerto Rico Highways and Transportation Authority (PRHTA) and the Puerto Rico Employees Retirement System (ERS).  

On July 2, 2017, the Oversight Board filed a petition under Title III of PROMESA in the United States District Court for the District of Puerto Rico, commencing a Title III case for the Authority.  

In a Title III case, the Oversight Board acts as the representative of the debtor and is authorized to take any actions necessary to prosecute the Title III case. See PROMESA § 315. Immediately upon filing the Title III petition, the broad automatic stay of Bankruptcy Code section 362 (which is incorporated into Title III cases under PROMESA) applies to automatically stay substantially all litigation against the debtor. After the Title III case is commenced, the Chief Justice of the
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United States Supreme Court must designate a district court judge to sit by designation and preside over the Title III case. PROMESA also provides that the commencement of a Title III case "does not limit or impair the powers of a covered territory to control by legislation or otherwise the exercise of the political or governmental powers of the territory or territorial instrumentality. . . ." PROMESA § 303.

(iv) Title IV — Temporary Stay of Litigation, Government Reporting, and Other Miscellaneous Provisions

Title IV of PROMESA contains several miscellaneous provisions, including a temporary stay of litigation related to "Liability Claims," relief from certain wage and hour laws, the establishment of a Congressional Task Force on Economic Growth in Puerto Rico (the "Task Force"), the requirement that the Comptroller General of the United States submit two reports to Congress regarding the public debt levels of the U.S. territories, and expansion of the federal government's small business HUBZone program in Puerto Rico.

Pursuant to PROMESA section 405, the enactment of PROMESA immediately and automatically imposed a temporary stay (the "PROMESA Stay") from June 30, 2016 (the date of PROMESA’s enactment) through February 15, 2017 of all "Liability Claim" litigation commenced against the government of Puerto Rico and its instrumentalities after December 18, 2015. See PROMESA § 405(d)(1)(A). A "Liability Claim" is defined as any right to payment or equitable remedy for breach of performance related to "a bond, loan, letter of credit, other borrowing title, obligation of insurance, or other financial indebtedness for borrowed money, including rights, entitlements, or obligations whether such rights entitlements, or obligations arise from contract, statute, or any other source of law related [thereto]" for which the Commonwealth or one of its instrumentalities was the issuer, obligor, or guarantor and such liabilities were incurred prior to June 30, 2016. PROMESA § 405(a)-(b). The PROMESA Stay as subject to a one-time 75-day extension by the Oversight Board or a one-time 60-day extension by the district court. On January 28, 2017, the Oversight Board extended the stay by 75 days to May 1, 2017, at which time the PROMESA Stay expired. Any party subject to the PROMESA Stay could have filed a motion in the United States District Court for the District of Puerto Rico seeking a relief from the PROMESA Stay upon "cause shown." PROMESA § 405(e).

Title IV of PROMESA also required several federal government reports. First, PROMESA established the Task Force within the legislative branch of the United States Government. See PROMESA § 409(a). On or before December 31, 2016, the Task Force was required to file a
report of findings regarding impediment in federal law and programs to Puerto Rico’s economic
growth and recommendations to “spur sustainable long-term economic growth.” PROMESA §
409(g).

Second, PROMESA required the U.S. Comptroller General, through the Government
Accountability Office (“GAO”), to submit a report to the House and Senate by December 30,
2017 regarding: (i) the conditions that led to Puerto Rico’s current level of debt; (ii) how
government actions improved or impaired its financial condition; and (iii) recommendations on
new fiscal actions or policies that the Government could adopt. See PROMESA § 410. The
GAO published this report on October 2, 2017.

Third, PROMESA required the U.S. Comptroller General, through the GAO, to submit to
In addition to its initial report, the GAO must submit to Congress updated reports on the public
debt at least once every two years. The GAO published this report on June 29, 2017.

(v) Title V — Infrastructure Revitalization

Title V of PROMESA establishes the position of Revitalization Coordinator under the Oversight
Board and provides a framework for infrastructure revitalization through an expedited permitting
process for “critical projects” as identified by the Revitalization Coordinator. See PROMESA §
502(a). Under PROMESA section 502(b)(1), the Oversight Board is required to submit at least
three nominees from which the Governor may appoint the Revitalization Coordinator. If the
Governor does not select a Revitalization Coordinator within 10 days after receiving the
nominations, the Oversight Board may appoint the Revitalization Coordinator by majority vote.
See PROMESA § 502(b)(1)(C). On October 30, 2016, the Oversight Board submitted the names of
three candidates to then-Governor García-Padilla for potential designation as Revitalization
Coordinator. On November 9, 2016, then-Governor García Padilla appointed Aaron Bielenberg
as Revitalization Coordinator. On July 24, 2017, in consultation with the Oversight Board,
Governor Rosselló Nevares appointed Noel Zamot to replace Mr. Bielenberg as Revitalization
Coordinator.

Under PROMESA section 501(2), a “critical project” means “a project identified under the
provisions of [Title V] and intimated related to addressing an emergency whose approval,
consideration, permitting, and implementation shall be expedited and streamlined according to
the statutory process provided by Act 76, or otherwise adopted.” An “emergency” means “any
event of grave problem of deterioration in the physical infrastructure for the rendering of
essentially to the people, or that endangers the life, public health, or safety of the population or of a sensitive ecosystem. . . . including problems in the physical infrastructure for energy, water, sewer, solid waste, highways or roads, ports, telecommunications, and other similar infrastructure.”

PROMESA § 501(5). Any party proposing an infrastructure project may submit a proposed project to the Revitalization Coordinator for consideration as a “critical project,” which submission must include the elements described under PROMESA section 503(a)(1).

Within 20 days after receiving the submission, each identified Commonwealth agency must submit to the Revitalization Coordinator its expedited permitting process for the proposed project. See PROMESA § 503(a)(3)(A). Within 60 days after receiving a submission, the Revitalization Coordinator must develop a “Critical Project Report” for each submitted project in consultation with the Governor and relevant Commonwealth agencies. See PROMESA § 503(b)(1). The Critical Project Report shall thereafter be published to allow at least 30 days of public comments. See PROMESA § 503(b)(2). After responding to public comments, the Revitalization Coordinator then submits the Critical Project Report to the Oversight Board, which shall approve or disapprove the project. See PROMESA § 503(c).

(vi) **Title VI — Consensual, Out-of-Court Restructuring Process**

Title VI of PROMESA establishes an out-of-court process for restructuring Puerto Rico’s debts. Under PROMESA section 601(d), the Oversight Board is authorized to establish “pools” of bonds issued by each Puerto Rico government-related issuer based upon relative priorities. After establishing the pools, the government issuer or any bondholder or bondholder group may propose a modification to one or more series of the government issuer’s bonds. If a voluntary agreement exists, the Oversight Board must issue a certification that: (i) the voluntary agreement conforms to the certified fiscal plan; (ii) if no fiscal plan has been certified, the voluntary agreement provides for a sustainable level of debt; or (iii) the voluntary agreement is limited to an extension of principal and interest payments on affected bonds for a period of one year. See PROMESA § 104(i). If a voluntary agreement exists, then the Oversight Board must certify the agreement as a “Qualifying Modification” by finding that either: (i) the issuer consulted with the holders of bonds in each pool prior to solicitation, all holders in each pool will be offered the same amount of consideration under the agreement, and the agreement is in the “best interest of the creditors and is feasible”; or (ii) the voluntary agreement has been entered into by a majority of the bondholders, all holders in each pool will be offered the same amount of consideration under the agreement, and the voluntary agreement is consistent with any restructuring support agreement executed prior to the establishment of the Oversight Board. See PROMESA § 601(g).
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If the voluntary agreement is certified as a “Qualifying Modification,” then the issuer must provide to the Calculation Agent, Information Agent, and Oversight Board additional information as required under PROMESA section 601(f).

Once the Oversight Board approves the voluntary agreement as a Qualifying Modification and the required information has been delivered, then the issuer, through the Information Agent, may solicit votes for bondholder approval of the Qualifying Modification. See PROMESA § 601(h). The Qualifying Modification will be deemed approved by bondholders if (x) of those who actual vote, at least two-thirds of the amount outstanding in each pool vote in favor of the Qualifying Modification, and (y) at least a majority of the aggregate principal amount of all bonds actually vote. See PROMESA § 601(j). After voting, in order for the Qualifying Modification to be conclusive and binding on all present and future bondholders:

- Each of the issuer’s bond pools must accept the Qualifying Modification based on the voting requirements above;
- The Oversight Board certifies that the voting requirements are satisfied, the Qualifying Modification complies with PROMESA § 104(i), and any conditions to effectiveness of the Qualifying Modification have been waived; and
- Rejecting, non-consenting secured lenders must retain their lien or receive value equal to the lesser of the amount of their claim or the value of the collateral securing such claim. See PROMESA § 601(m).

Finally, the United States District Court for the District of Puerto Rico must enter an order approving the Qualifying Modification and vesting in the issuer all property free and clear of claims in respect of any bonds. See PROMESA § 601(n).

The Title VI process is currently being implemented to restructure the debts of the GDB.

(vii) Title VII — Sense of Congress

Title VII of PROMESA sets forth the sense of Congress that “any durable solution for Puerto Rico’s fiscal and economic crisis should include permanent, pro-growth fiscal reforms that feature, among other elements, a free flow of capital between possessions of the United States and the rest of the United States.”
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(a) *Actions of the U.S. Government, Congress and Oversight Board after the Enactment of PROMESA*

1. Oversight Board Public Meetings

Pursuant to PROMESA section 104(a), the Oversight Board periodically holds public meetings to conduct its business and hear testimony regarding key developments in the Commonwealth’s restructuring efforts.

The Oversight Board has held public meetings, for a detailed description of the events of each meeting, see the information available on the Oversight Board’s public website located at: https://juntasupervision.pr.gov

2. Oversight Board Commencement of Title III Cases

On May 1, 2017, the PROMESA Stay expired, permitting the substantial litigation brought by bondholders and other creditors against the Commonwealth and its instrumentalities to resume. As a result, on May 3, 2017, the Oversight Board commenced a Title III case for the Commonwealth by filing a petition for relief under Title III of PROMESA. On May 5, 2017, the Oversight Board commenced a Title III case for COFINA by filing a similar petition for relief under Title III of PROMESA. On May 21, 2017, the Oversight Board commenced Title III cases for PRHTA and ERS by filing similar petitions for relief under Title III of PROMESA. On July 3, 2017, the Oversight Board commenced a Title III case for the Authority by filing a similar petition for relief under Title III of PROMESA. On May 11, 2017, United States Supreme Court Chief Justice John Roberts designated United States District Judge Laura Taylor Swain as the presiding judge in the Title III cases. All of the foregoing Title III cases have been consolidated for procedural purposes only and are being jointly administered under Case No. 17-3283-LTS in the United States District Court for the District of Puerto Rico.

The Title III cases were commenced in part due to the May 1 expiration of the PROMESA Stay. Title III of PROMESA incorporates the automatic stay provisions of Bankruptcy Code section 362 and 922, which are made applicable to the Title III cases pursuant to PROMESA section 301(a).

A discussion of the events in the Title III cases is provided below.

3. *Key Contested Motions in the Title III Cases*
   - Ad Hoc Group of PREPA Bondholders’ Stay Relief Motion
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On July 18, 2017, certain financial creditors of the Authority filed a motion seeking to lift the automatic stay in the Authority’s Title III case to file an action in the Commonwealth court seeking the appointment of a receiver for the Authority to oversee certain operations of the utility company, and to seek an increase in rates. The motion was filed by National Public Finance Guaranty Corp., the Ad Hoc Group of PREPA Bondholders, Assured Guaranty Corp. and Syncora Guarantee Inc.  

On September 15, 2017, Judge Swain denied the Ad Hoc Group of PREPA Bondholders’ motion seeking to lift the PROMESA’s law’s stay. In her determination, Judge Swain concluded that the PREPA Bondholders failed to demonstrate cause for lifting the automatic stay that would have allowed the PREPA Bondholders to seek the appointment of a receiver for the Authority. Judge Swain found that relief sought by the Bondholders, which was expressly designed to facilitate an increase in electricity rates, would run counter to PROMESA’s designation of the Authority as the sole entity empowered to develop and propose a plan of adjustment. The Ad Hoc Group of PREPA Bondholders have appealed Judge Swain’s determination, which appeal is currently pending.  

- **Aurelius’ Motion to Dismiss the Title III Petitions**

On August 7, 2017, a group of GO bondholders led by Aurelius Investment, LLC, Aurelius Opportunities Fund, LLC and Lex Claims, LLC (collectively, “Aurelius”) filed a motion to dismiss the Title III petitions. In the motion, Aurelius argues that the appointment of the Oversight Board members violated the “Appointments Clause” of the United States Constitution, which requires that “principal officers” of the United States be appointed by the President and confirmed by the Senate. Aurelius contends that the Oversight Board members are “principal officers” and that they were not appointed by the President and confirmed by the Senate. As a result, Aurelius claims that the act of the Oversight Board are void because an invalidly constituted Oversight Board issued the restructuring certifications and filed the petitions commencing the Title III cases. AAFAF, the Oversight Board, the Official Retiree Committee, the Official Committee of Unsecured Creditors, the COFINA Senior Bondholders’ Coalition, and AFSCME filed motions opposing Aurelius’ motion on November 3, 2017. On November 6, 2017, the U.S. Department of Justice informed the Title III court that it intends to intervene and will file an objection brief by December 6, 2017. On November 20, 2017, Aurelius filed a reply brief in further support of its motion to dismiss. A hearing on the motion is currently scheduled for January 10, 2018.  

- **Oversight Board’s Motion to Appoint a Chief Transformation Officer for the Authority**
On October 26, 2017, the Oversight Board filed a motion (the “CTO Motion”) seeking an order to confirm its appointment of Noel Zamot as the Chief Transformation Officer for the Authority (the “CTO”). Under this appointment, Mr. Zamot would have essentially displaced the Authority’s Executive Director and Governing Board by assuming all management and control of the business and affairs of the Authority, while reporting solely to the Oversight Board rather than the Governor.

The issue at the heart of the CTO Motion was whether PROMESA grants the Oversight Board authority to unilaterally displace a statutorily-created management structure and direct the executive functions of a Title III debtor. In the CTO Motion, the Oversight Board argued that, given the Authority’s pivotal role in the overall Commonwealth restructuring, the Oversight Board should have sufficient powers under PROMESA to control the Authority’s operations to ensure that restructuring goals are met. In response, AAFAF, on behalf of the Authority, argued that the Oversight Board has no power under PROMESA to manage and control the day-to-day activities of any Commonwealth entity, which powers are specifically reserved to the Commonwealth government and are outside the Oversight Board’s powers under PROMESA. At a hearing held on November 13, 2017, Judge Swain denied the CTO Motion. On November 28, 2017, the Oversight Board issued a press release stating that it will not appeal Judge Swain’s decision.

**Key Legislation After the Enactment of PROMESA**

**Act 2-2017**

Act No. 2 of January 18, 2017 (“Act 2-2017”) was enacted to repeal and replace the sections under the Moratorium act that established AAFAF and its powers and responsibilities. Act 2-2017 expanded AAFAF’s powers so that it has the sole responsibility to renegotiate, to restructure and to reach agreements with creditors on all or part of the public debt or any other debt issued by any Commonwealth entity. In addition, AAFAF is the entity in charge of the collaboration, communication and cooperation efforts between the Commonwealth and the Oversight Board under PROMESA. In essence, Act 2-2017 established AAFAF as the Commonwealth entity responsible for carrying out the roles inherited from the GDB along with additional duties and powers, which include, among other things:

- *Overseeing the Commonwealth Budget.* AAFAF must ensure compliance with the fiscal plans and budgets certified by the Oversight Board pursuant to PROMESA.
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- **Administrative Presence.** AAFAF’s executive director will be represented on every board, committee, or organism where the GDB president is currently a member. 

- **Auditing.** AAFAF has the authority to conduct audits and investigations, including requesting information, as part of its oversight efforts. 

- **Managing.** If any overspending is detected, AAFAF is authorized to freeze budgetary items, appoint trustees, redistribute human resources, and change procedures, among other actions.  

In connection with the expanded powers granted to AAFAF through Act 2-2017, AAFAF issued Administrative Order ("AO") 2017-01, which ordered a freeze on disbursing approximately $1.8 billion in special assignments approved throughout the years by the Legislative Assembly, as well as a freeze in processing tax credits that have not yet been approved by the Treasury Department. In addition, a committee consisting of representatives from AAFAF, the Treasury Department, and the OMB was established to determine which disbursements of special assignments and tax credit grants will be made in the future based on the current administration’s criteria for essential services. 

On May 15, 2017, AAFAF issued AO 2017-02, which, among other things, announced the following directives geared toward ensuring compliance with the liquidity and fiscal targets of the Certified Commonwealth Fiscal Plan:  

- **Instruct** agencies and instrumentalities within the Executive Branch of the Commonwealth to present a detailed report with the efforts made and savings goals achieved pursuant to all the executive orders already issued by the Governor. 

- **Request** that the Secretary of the Treasury Department create the Additional Cash Reserves set forth in the March 13 Commonwealth Fiscal Plan, which will be under its custody and maintained in a bank account separate from the Commonwealth’s TSA. 

- **Instruct** the agencies and instrumentalities of the Commonwealth to deposit into the aforementioned Additional Cash Reserves account all the savings achieved pursuant to the Governor’s executive orders.
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Act 5-2017  

On January 29, 2017, Governor Rosselló Nevares signed into law Act No. 5 of 2017, known as the Puerto Rico Fiscal Responsibility and Financial Emergency Act ("Act 5-2017"), which amended and repealed certain provisions of the Moratorium Act. Act 5-2017 maintained the moratorium on debt payment existing under the Moratorium Act; however, it allowed the Commonwealth to segregate funds that would eventually be used to fund the payment of public debt.

Sections 201 and 202 of Act 5-2017 state that the Governor will pay debt service as long as the Commonwealth could continue to fund essential services, such as the health, safety, and well-being of the people of Puerto Rico, including providing for their education and assistance to residents. Act 5-2017 also maintained most of the prohibitions existing under the Moratorium Act regarding loan disbursements by GDB and most of the procedures with respect to governmental withdrawals, payments, and transfer requests in respect of funds held on deposit at GDB. Act 5-2017 continued to declare the Commonwealth to be in a state of emergency and increased the Governor’s powers to manage the Commonwealth’s finances. Some of these additional powers included:

- Exercising receivership powers to rectify the financial emergency declared by the Moratorium Act and Act 5-2017, which may include, among other actions, limiting expenditures of appropriated funds, issuing executive orders regarding the disbursement or disposition of funds held by GDB, accepting or rejecting any executory contracts, approving or disapproving of any debt obligation plans, reviewing and approving of payrolls or other claims against the Commonwealth before payment, and appointing and removing the heads of Commonwealth entities within the Executive Branch that are employees of trust and confidence,

- Exercising general supervisory control over the functions and activities of all government entities within the Executive Branch,

- Initiating court proceedings in the name of the Commonwealth to enforce compliance with any constitutional mandate or requirement of Act 5-2017,

- Issuing executive orders to implement and enforce compliance with Act 5-2017, and
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- Hiring of or contracting with government workers or professional persons who would not be subject to certain laws, as defined.

The emergency period under Act 5-2017 was set to expire on May 1, 2017 to coincide with the expiration of the temporary stay under PROMESA section 405 (as discussed above), unless extended by an additional three months by executive order.

On April 30, 2017, the Governor issued executive order OE-2017-031, which extended to Act 5-2017 emergency period to August 1, 2017. On July 19, 2017, the Legislative Assembly enacted Act No. 46-2017 (“Act 46-2017”), which further extended the Act 5-2017 emergency period through December 31, 2017. Act 46-2017 allowed the Governor to sign executive orders to extend the emergency period for successive periods of six months as long as the Oversight Board remains established for Puerto Rico under PROMESA.

Act 37-2017

On June 26, 2017, Governor Rosselló Nevarez signed into law Act No. 37 of 2017 (“Act 37-2017”) in order to overhaul the Authority’s then-existing governing board structure. Since the enactment of Act 37-2017, the Authority’s governing board (the “Governing Board”) consists of seven members. Of its seven-member board, six members are designated by the Governor (three of which require Senate approval) and one member will be an elected consumer representative.

The Authority’s Fiscal Plan

On March 13, 2017, the Authority presented its 10-year fiscal plan to the Oversight Board. Faced with the challenges referred to above but capitalizing on the then-existing RSA (as described below), the Authority’s fiscal plan commits to fiscal responsibility and implements urgently needed infrastructure modernization, public-private partnerships, targeted expenditure reductions/efficiencies (operational and other) and specific revenue enhancements to return the Authority to (i) fiscal stability, (ii) efficient and competitive energy prices, (iii) compliance with environmental and health standards, and (iv) being an agent of economic growth. In particular, the fiscal plan contemplated revised fuel prices, distributed generation trends, urgent infrastructure investments for needed efficiencies and environmental compliance, operational transformation to benefit its customers and Puerto Rico’s economy. More specifically, the Authority’s fiscal plan addressed the following revised areas:
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- Ensured that the fiscal plan’s underlying baseline forecasts are now aligned with the central government macroeconomic assumptions.

- Lowered demand and volume baseline projections to align with historical trends of a decline in consumption.

- Incorporated latest terms of the RSA, reflected debt service, and determined uses of increased liquidity.

- Detailed investment program, including funding gap, total cost, major projects and timeline.

- Adopted a formula rate mechanism and ensure alignment between the Puerto Rico Energy Commission and the Authority.

- Addressed CILT spending to municipalities.

- Broadened operational savings to include further labor, maintenance strategy and time, and distribution savings.

- Targeted additional fuel savings by driving generation efficiency.

- Demonstrated measures that enable corporate governance to improve compliance and visibility of plan.

On April 28, 2017, the Oversight Board approved the fiscal plan for the Authority, subject to the following amendments:

*Amendment 1:*

- Based on the review and analysis of the proposed fiscal plan, energy prices in comparable and competitor jurisdictions, and the best available projections, the Oversight Board believes the Authority’s Fiscal Plan must be amended to contain achievable, credible, necessary changes to deliver energy to ratepayers at an average all-in rate of 21 cents per kWh by 2023 (the “Target Rate”). The Target Rate reflects the projections of demand, inflation, fuel prices and other
external factors included in the fiscal plan. To the extent these factors are different in 2023, the target rate may need to be adjusted (e.g. higher fuel prices may require somewhat higher rates, higher demand may provide for lower rates).

- To deliver power at the Target Rate, the Authority will need to substantially lower the cost of generating power (fuel costs) and improve the distribution grid through unimpeded public/private partnerships agreements and/or fully privatizing energy generation subject to regulated utility standards.

- The Authority’s Fiscal Plan targets are amended consistent with the aforementioned goals, which were reflected in a revised Fiscal Plan document submitted to the Oversight Board. The Authority developed and submitted to the Oversight Board a specific implementation plan to deliver power to rate payers at the Target Rate by 2023 through lower costs of generation and other efficiencies. The implementation plan reflected:

  - A clear path to realizing necessary capital improvements expeditiously, including a workable financing strategy for a credible capital expenditures plan that rapidly transitions the generation mix to lower cost power sources.

  - A detailed plan to implement public/private partnerships or full privatization for energy generation and to finance necessary improvements in the grid.

  - Changes to improve operational efficiency and procurement practices, lower pension costs, reduce contract spending, and lower other costs.

  - Development and inclusion of a detailed elimination of the CILT to 0% within the next 3-5 years beyond the 15% reduction included within the Authority’s Fiscal Plan.

  - A review of assets that could be monetized, either in the context of public private partnerships or otherwise, to fund necessary capital improvements.
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Amendment 2:  
- The Authority’s Fiscal Plan should be amended to include a requirement to provide to the Oversight Board a confirmation that the composition of its board shall be in compliance with the requirement that at least two thirds of its members meet the qualifications of independence and expertise in energy matters.  

Amendment 3:  
- The Authority’s Fiscal Plan should be amended to include a requirement to initiate a 60-day process to establish a mechanism for rate approval with the Puerto Rico Energy Commission reflecting the Formula Rate Mechanism (“FRM”) and rate structures to be determined necessary to meet the amended fiscal plan Target Rate, which shall need to be consistent with the annual Authority budgets to be certified by the Oversight Board. The Authority should work with the Puerto Rico Energy Commission and provide to the Oversight Board within 30 days of this certification an implementation plan for the FRM to be reviewed and approved by the Oversight Board before its submittal for approval by the Puerto Rico Energy Commission.  

In light of Hurricane María, the Oversight Board has requested that all certified fiscal plans be modified to take into consideration the new financial reality in Puerto Rico. An amended and restated draft version of the Authority’s fiscal plan was submitted to the Oversight Board on April 5, 2018.  

Forbearance Agreements  

On August 14, 2014, the Authority entered into certain forbearance agreements (collectively, the “Forbearance Agreements”) with certain insurers (the “Monoline Bond Insurers”), beneficiary owners of Power Revenue Bonds (the “Ad Hoc Group of Bondholders”), banks that provide fuel lines of credit (collectively, the “Forbearing Lenders”), and the GDB (collectively, the “Forbearing Creditors”). As provided in the Forbearance Agreements, the Forbearing Creditors agreed not to exercise certain rights and remedies under their financing agreements. The Authority also agreed to prepare a new business plan, 13-week cash flows, and a recovery plan that would be acceptable to the Forbearing Creditors.
The Forbearance Agreements were scheduled to terminate originally on or before March 31, 2015, but were extended on numerous occasions, most recently through November 5, 2015.

The Forbearance Agreements expired on November 5, 2015, but the agreement of the Forbearing Creditors to refrain from exercising certain rights and remedies was extended under the RSA (as defined and discussed below).

Under the Forbearance Agreements, as extended and continued under the RSA, the Authority’s obligations to pay any and all principal and interest payments on the Power Revenue Bonds continued. The Forbearing Bondholders consented to an amendment to the Trust Agreement (the “Trust Agreement Amendment”) permitting the Authority not to make transfers to the Revenue Fund or the Sinking Fund pursuant to sections 506 and 507 of the Trust Agreement while the Trust Agreement Amendment, as extended and continued under the RSA, remained in effect. The Authority has not made monthly cash deposits into the Sinking Fund through January 2017, and then defaulted on the payments due on July 3, 2017 and January 2, 2018, shortly before and after the commencement of the Authority’s Title III case.

Under the Forbearance Agreements, as extended and continued under the RSA, the Authority was also permitted to delay making certain payments that became due to the Fuel Line Lenders in July and August 2014.

In order to address the Authority’s liquidity challenges, the Trust Agreement Amendment permitted the Authority to use approximately $280 million held in its construction fund for payment of current expenses in addition to capital improvements. The Amendment also provided for an increase in the thresholds required for the exercise of remedies under the Trust Agreement. In connection with the continued implementation of the RSA, the Trust Agreement was again amended to allow for the issuance of $130.7 million in bonds to the Monoline Bond Insurers that would mature on January 1, 2016.

On July 1, 2015, the Authority paid, as required by the Forbearance Agreement, $415.8 million to satisfy the principal and interest payments on the bonds due on that date. This payment was funded with moneys in the 1974 Sinking Fund, including reserves, and a $153.0 million transfer from the Authority’s General Fund.
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On July 31, 2015, pursuant to the Trust Agreement and as agreed with Forbearing Creditors, the Authority issued Power Revenue Bonds Series 2015A (the “Series 2015A Bonds”), in a par amount of $130.7 million, to be used as working capital. The Series 2015A Bonds were purchased in their entirety by current bond insurers, and the maturity date of this issue was January 1, 2016.

In accordance with the terms of the Series 2015A Bonds, the Authority made several mandatory redemption payments prior to maturity. On December 15, 2015, the Authority deposited $103.5 million in escrow to satisfy the remaining principal and interest requirements on the Series 2015A Bonds, which deposit was funded by $100.9 million from the Authority’s selfinsurance fund and $2.6 million from the Authority’s General Fund. These amounts were paid to holders of the 2015A Bonds on January 4, 2016 in accordance with their terms.

Also on January 4, 2016, the Authority paid $198.0 million, to satisfy the interest payments on its other outstanding Bonds due on that date. This payment was funded with moneys in the 1974 Sinking Fund, and a $171.0 million transfer from the General Fund.

On July 1, 2016, the Authority paid $416 million to satisfy the principal and interest payments on its Bonds due on that date. This payment was funded with moneys in the Sinking Fund, approximately $264 million in proceeds from the sale of the 2016 CDE Bonds (referred to below) to certain Forbearing Creditors and a $146.8 million transfer from the General Fund.

On January 3, 2017, the Authority paid $197.7 million, to satisfy the interest payments on its other outstanding Bonds due on that date. This payment was funded with $194.4 million transfer from the General Fund.

The Authority did not make the principal and interest payments due on the Bonds on July 3, 2017.

Agreements in Principle with Certain Creditors

On September 2, 2015, the Authority announced an agreement in principle regarding the economic terms of a restructuring with the Ad Hoc Group of Bondholders that were Forbearing Bondholders (the “Ad Hoc Group Agreement”) and which group held, at that time, approximately 35% in principal amount of the outstanding Bonds, which agreement was incorporated into the RSA. On September 22, 2015, the Authority announced an agreement in principle regarding economic terms with its Forbearing Lenders (the “Fuel Line Agreement”).

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Under the extensions to the Forbearance Agreements with the Forbearing Lenders executed on September 22, 2015, the Authority agreed to work collaboratively and in good faith with the Forbearing Lenders to reach agreement on a recovery plan incorporating these terms. The Fuel Line Agreement was included in the RSA.

**Restructuring Support Agreement**

On November 5, 2015, the Authority announced its entry into a restructuring support agreement (the “Initial RSA”) with both the Ad Hoc Group (representing at that time approximately 40% in principal amount of the outstanding Bonds) and the Forbearing Lenders setting forth the agreed-upon terms of the Authority’s recovery plan, which terms were amended to extend the milestone dates therein on numerous occasions. On December 23, 2015, certain of the Monoline Bond Insurers along with the Ad Hoc Group (representing together at that time approximately 66% in principal amount of the outstanding Bonds), the Forbearing Lenders and GDB (the “Supporting Creditors”), all signed an amended and restated version of the Initial RSA (the “A&R RSA”).

On January 23, 2016, the A&R RSA terminated when the PREPA Revitalization Act was not enacted into law and the Ad Hoc Group did not agree to the Authority’s request to extend the related milestone. The Authority continued to engage in discussions with the Ad Hoc Group and the other Supporting Creditors regarding a potential extension of the A&R RSA.

On January 23, 2016, certain of the Forbearing Lenders agreed to enter into a short form forbearance agreement by which they agreed to forbear from exercising enforcement rights against the Authority under the applicable fuel line agreements through February 12, 2016.

On January 27, 2016, the Authority and the Supporting Creditors executed a revised restructuring support agreement (the “RSA”) that was substantially the same as the A&R RSA, with minor adjustments to address delays in legislative consideration of the PREPA Revitalization Act.

Starting on June 22, 2016, the Authority and the Supporting Creditors executed three supplements to the RSA that (i) extended the December 15, 2016 termination date, (ii) revised certain milestone dates, (iii) reduced forbearance fees, and (iv) added a new milestone for reaching an agreement on amendments to the RSA necessary to implement the transactions contemplated therein under a mechanism agreeable to the parties on or before January 31, 2017 (the “Implementation Milestone”).
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On January 27, 2017, AAFAF advised the Authority that pursuant to Act 2-2017 it assumed all responsibilities for negotiations with the Authority’s creditors and requested that the Authority agree to extend the Implementation Milestone to provide AAFAF additional time to review the terms and conditions of the RSA.

Thereafter, the parties to the RSA entered into 15 additional supplements that ultimately extended the termination date and Implementation Milestone to June 28, 2017.

However, the RSA was subject to the approval of the Oversight Board under PROMESA, and the Oversight Board declined to approve the RSA on June 27, 2017. As a result, the RSA terminated by its own terms on June 29, 2017.

Oversight Board Actions

As noted above, the RSA was subject to approval of the Oversight Board under PROMESA. After consideration of the terms of the RSA, the Oversight Board ultimately declined to approve the RSA on June 27, 2017, and the RSA expired and terminated by its terms on June 29, 2017. On June 30, 2017, the Governor submitted a letter to the Oversight Board stating that the Authority desired to effect a plan to adjust its debts under Title III of PROMESA as a result of the rejection of the RSA and the lack of a stay under PROMESA. On July 2, 2017, the Oversight Board filed a petition under Title III of PROMESA in the United States District Court for the District of Puerto Rico, commencing a Title III case for the Authority.

Bond Ratings Downgrades

Since June of 2014, the credit ratings of the Authority’s Power Revenue Bonds, already within noninvestment grade, have been lowered (more than once in most cases) by Moody’s and S&P. On September 17, 2014, Moody’s downgraded the Authority’s bond rating from Caa2 to Caa3. On July 2, 2015, S&P lowered the Authority’s bonds from CCC to CC. Fitch has maintained its rating on the Authority’s bonds at CC since June of 2014. On July 1, 2016, again S&P lowered the Authority’s bond ratings from CC to D. On June 27, 2016, Fitch lowered its rating on the Authority’s bonds from CC to C. These downgrades consider the uncertainty that persists regarding the details of the expected restructuring plan by the Authority, anticipation of distressed debt exchanges and the implementation risk that continues regarding the Authority’s ability to execute on its multiyear fuel conversion plan as well the rating agencies’ belief that any such debt restructuring will involve some degree of impairment for bondholders. The
downgrades also reflect the concerns raised by: (i) the repeated draws on the debt reserve fund and uncertainty regarding any future draws that could result in its depletion; (ii) the structural imbalance between revenue and expenses without a pathway to meeting debt service obligations; and (iii) the inability of the Authority to access the capital markets.

On July 6, 2017, Moody’s again downgraded its rating for the Authority’s bonds to Ca from Caa3, with the outlook remaining negative. This latest downgrade reflects the Authority having commenced a proceeding under Title III of PROMESA. At the same date, Fitch also downgraded its rating for the Authority’s bonds to D. As of April 20, 2018, the ratings remained the same.

**Palo Seco Plant**

In June 2016, an assessment of the structural steel that supports the boilers of Palo Seco Steam Plant, units 1 to 4, was made by Mr. William R. Schlumpf, a licensed Professional Engineer with over 34 years of experience in all aspects of design and construction of power, industrial and commercial projects. At the time of the assessment Mr. Schlumpf was working with Sigma Energy Solutions Inc., a subsidiary of Alstom (now General Electric), the manufacturer of the Authority’s boilers and original designers of its supporting structures. In conclusion, the assessment indicates that there are areas with critical deficiencies among other safety and operational issues.

In August 2016, the Authority received a proposal from General Electric Inc., to rehabilitate and repair the deficiencies of the structural steel at the Palo Seco units and subsequently, a planning and negotiation process began. On November 2017, General Electric and the Authority signed the contract of the repairs project.

On August 18, 2017, the island was impacted by a strong seismic event before the contract was settled. The Authority requested a damage assessment to reevaluate the structural elements for any significant condition changes.

The impact of the seismic event was minimal, but the degradation by corrosion in the structural elements is at a critical level, with 25% of its original design thickness in the column bases. After evaluating the risks and consequences, the Authority decided to remove the personnel and stop generating from the Palo Seco Steam Plant.
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On September 6, 2017, the island was severely affected by Hurricane Irma and on September 20, 2017 devastated by Hurricane María. The Authority decided to perform another damage assessment on the structural steel. This was done also before signing the contract.

Those damages assessments were necessary to identify significant impacts in the structural steel that could increase the risks for the structures to an imminent collapse and consequently, the terms and conditions of a contract.

No change to the contract’s scope, terms and conditions was necessary at this time. The planning for the repairs continued the same as initially stated and it is expected that after beginning the execution, the most critical areas will be repaired within the first 60 days.

After completing ground level repairs on units 3 and 4, the Steam Plant will be reopened to its normal operations, controlling and limiting personnel access in several areas. The structural repairs project in Palo Seco Plant units is scheduled to be completed in seven months. As of April 20, 2018, the Palo Seco Plant units were at 27% capacity of power generation.

The contract for the structural steel repairs in the Palo Seco Steam Plant was signed on October 12, 2017. A preexecution meeting was performed on October 24, 2017, and an agreement for mobilization was made the following week.

**Hurricane Irma**

On September 5, 2017, the Authority declared an emergency that activated the Emergency Operations Center, the Technical Operations Center, and the Regional Operations Center address expected operational challenges due to Hurricane Irma approaching Puerto Rico. On September 6, 2017, Hurricane Irma passed just north of San Juan, Puerto Rico as a Category 5 hurricane. On September 7, 2017, the Authority partially lifted the emergency status to include only the operations directorates.

As a result of Hurricane Irma, customer power outages reached their highest point on September 7, 2017 with approximately 1.1 million (or 75 percent) of customers without power. The lowest point of customer power outages due to Hurricane Irma occurred on September 14, 2017 with approximately 93,650 (or 6.2 percent) of customers without power. As of September 14, 2017, 12 municipalities were declared Disaster Zones, as a result of the destruction caused by Hurricane Irma, with the possibility of adding others.
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As of September 15, 2017, the Authority was in the process of evaluating the extent of the damages to the system and quantifying the costs of the emergency and repairs to the system. Additionally, the Authority is working closely with the Federal Emergency Management Agency (“FEMA”) to ensure adequate documentation of the costs of the emergency and repairs. The Authority already informed and is currently working in a property insurance claim to its insurers.

Hurricane María

On September 18, 2017, the Authority declared an emergency that activated the Emergency Operations Center, the Technical Operations Center, and the Regional Operations Center to address expected operational challenges due to Hurricane María approaching Puerto Rico. On September 20, 2017, Hurricane María made landfall in Puerto Rico as a Category 4 hurricane.

As a result of Hurricane María, customer power outages reached its highest point on September 20, 2017 with 1.4 million (or 100 percent) of customers without power. As of the date of these financial statements, the percentage of customers without power was 2.85 percent. On October 4, 2017, all of the Commonwealth’s 78 municipalities were declared Disaster Zones. The Authority is currently in the process of assessing the extent of damages to the System and quantifying the costs of repairing and rebuilding the System. Additionally, the Authority is working closely with FEMA to ensure adequate documentation of the costs of the emergency and repairs. The Authority has submitted and is currently working in a property insurance claim to its insurers.

Impact of Hurricanes Irma and Maria

The Authority’s electric system sustained significant damage as a result of Hurricanes Irma and Maria. The damages were exacerbated by the fact that the Authority’s infrastructure was in disrepair prior to the hurricanes, due to years of limited investment and lack of maintenance. Hurricane María brought sustained winds of 155 miles-per-hour and significant rainfall over a 30-hour period. Hurricane María crossed Puerto Rico diagonally, entering through the Southeast and exiting through the Northwestern region. The hurricane caused catastrophic destruction in Puerto Rico, including severe damage to the electric power system, and left the island completely without power. Only two weeks prior to Hurricane María, Hurricane Irma—one of the strongest hurricanes ever recorded in the Atlantic—passed by Puerto Rico’s north coast, substantially impairing an already weak infrastructure.
After Hurricane Maria passed through the island, and when it was safe for personnel to return to the field, the Authority deployed assessment teams to conduct a preliminary damage assessment and attempted to re-establish communications with the Authority’s various key components. This initial assessment confirmed that the Authority’s entire grid suffered severe damage. The infrastructure was designed to withstand winds up to 140 miles per hour, but Hurricane Maria brought sustained winds of approximately 155 miles per hour. This resulted in massive direct damage, mechanical fatigue, and stress that will require significant repairs and/or replacement of the following systems, among other things:

- **Transmission:** Hundreds of major transmission structures were damaged, and hundreds of hardware, conductor, and insulator failures were also identified at that time.

- **Distribution:** Many thousands of individual distribution lines, poles, and transformers were felled or damaged, which will require debris removal and line reconstruction and repair.

- **Communications and IT:** Communications and IT systems throughout much of the Authority’s system were not functional in the immediate aftermath of Hurricane Maria. The Authority’s datacenter, which houses the Authority’s critical IT assets, was offline for weeks. Internet communication was non-existent for the first two weeks and intermittent thereafter. Most of the communication antennas suffered severe damage. During the weeks after the hurricane, the Authority had to rely on several short-wave radios and satellite phones for its limited communication abilities.

Based upon the damage assessment, the Authority began implementation of its emergency communication and restoration procedures. The Authority established five key stabilization initiatives essential to the emergency response: (1) reestablishing communications and IT systems, (2) reconstructing distribution and transmission systems, (3) energizing substations, (4) procurement and liquidity, and (5) operations planning.

The Authority’s initial recovery actions focused on re-establishing power to the most critical customers including: (i) hospitals and elder care facilities; (ii) airports; (iii) ports; (iv) water and sewage treatment plants; (v) agencies providing essential services; (vi) lodging facilities; (vii) industrial buildings; (viii) financial institutions; and (ix) ice-making plants.
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The Authority also requested representatives from FEMA and other critical stakeholders to be present at the Authority’s headquarters on a regular basis to be part of an integrated working group to expedite execution of the Authority’s emergency response plan. This group and other key personnel coordinated daily in the immediate aftermath of the hurricanes.

As of April 20, 2018, Puerto Rico’s main metropolitan cities have power to their hospitals, ports, airports and water & sewage infrastructure. Approximately 97.4% of instant maximum load has been restored. Moreover, approximately 95.0% of substations are operational, and 99.4% and 99.7%, in the Ponce and San Juan regions, respectively, and 100% of the other five regions, of the “feeders” —the major distribution lines emanating from substations—are also operational. In addition, through this process, each substation was fully inspected and the Authority obtained detailed reports regarding maintenance and repair requirements for each station. These reports will allow the Authority to better focus the repair efforts and ensure the quickest avenue to restore power Island-wide.

The Authority closely monitors these ongoing efforts and deploys or re-deploys personnel and assets as necessary to ensure the continued path to recovery. The Authority prepares daily key performance indicator reports addressing the daily status of transmission, generation and distribution operations. These reports also assist in monitoring and strategizing on the load to keep the system running as smoothly as possible, and in allowing the Authority to align the efforts of the various contractors, the Authority’s personnel, and governmental agencies involved in the effort.

Announcement of Privatization of the Authority

On January 22, 2018, the Governor of Puerto Rico announced that the government will begin the transformation of the Puerto Rico Electric Power Authority (PREPA). The purpose of the transformation is to assure that the system is modern and reliable and that energy rates are affordable for the people of Puerto Rico. The contemplated transformation will involve; (a) private ownership and operation of generation assets and (b) an operator of the transmission and distribution system through a concession model. The transformation will likely be an 18-month to 2-year process.
Superpriority Post- Petition Revolving Credit Loan Agreement

On February 22, 2018, the Puerto Rico Electric Power Authority (the “Borrower”) and the Commonwealth of Puerto Rico (the “Lender”) entered into a Revolving Credit Loan Agreement, in which the Lender agreed to make a revolving loan to the Borrower consisting of a superpriority post-petition credit facility in an aggregate principal amount not to exceed $300 million, available to the Borrower until June 30, 2018, unless extended by necessary governmental action by the Lender. The Revolving Credit Loan shall bear 5% interest, provided that, in the event the Lender funds or refinances the Revolving Credit Loan with the proceeds of a Commonwealth Financing, the interest rate on the such funded or refinanced Revolving Credit Loan shall automatically accrue interest at the rate equal to the interest rate on the Revolving Credit Loan not funded or refinanced with any Commonwealth Financing. The Borrower shall pay the Lender from time to time the amount necessary so that the unpaid balance does not exceed the Revolving Loan Commitment then in effect.

Delegation of Powers to the Puerto Rico Fiscal Agency and Financial Advisory Authority (FAFAA) related to the Employees’ Retirement System

On March 22, 2018, the Governor of Puerto Rico issued Executive Order OE-2018-012 in which the Authority’s Governing Board was appointed receiver of the Employees’ Retirement System (the Retirement System) to: i) take those actions and decisions that are necessary to immediately finalize, evaluate, approve and/or sign the necessary documents (including the representation letter from the System’s management) for the final publication of the actuarial reports and audited financial statements of the Retirement System for the corresponding fiscal years, up to and including fiscal year 2017, and ii) deliver, or cause the delivery to FAFAA of any information of the Retirement System necessary or convenient for the elaboration of the Authority’s revised Fiscal Plan or budget for fiscal year 2019. This designation will be in effect until: i) the actuarial reports and audited financial statements of the Retirement System are issued for the corresponding fiscal years, up to and including fiscal year 2017, ii) the Financial Oversight and Management Board (FOMB) certifies a received Fiscal Plan for the Authority and iii) the FOMB certifies a budget for the Authority for fiscal year 2019. The Retirement System’s Board of Trustees will continue to exercise all other functions that correspond to it in the daily administration of the Retirement System, provided that, in no way may it directly or indirectly prevent, or allow the prevention through third parties, including contractors, of the approval and/or publication by the Authority’s Governing Board of the actuarial reports and financial statements of the Retirement System.
Pension Plan Financial Statements and Actuarial Report

On April 5, 2018, the PREPA Employee Retirement System re-issued the 2014 and 2015 financial statements and actuarial report as a result of revised actuarial valuation.
Required Supplementary Information
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Supplementary Schedule of Funding Progress-  
Postemployment Health Plan (Unaudited)  

Year Ended June 30, 2015  
(In million)  

<table>
<thead>
<tr>
<th>Actuarial Valuation Date</th>
<th>Unfunded Actuarial Accrued Liability (UAAL) (a)</th>
<th>Covered Payroll (b)</th>
<th>UAAL Percentage of Covered Payroll (a)/(b)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Postemployment Health Plan</td>
<td>$378</td>
<td>$365</td>
<td>104 %</td>
</tr>
<tr>
<td>07/01/2012</td>
<td>$408</td>
<td>$357</td>
<td>114 %</td>
</tr>
<tr>
<td>07/01/2008</td>
<td>$587</td>
<td>$363</td>
<td>162 %</td>
</tr>
</tbody>
</table>

*Postemployment Health Plan valuation performed every two years, as required by the GASB.*
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)

Schedule of Changes in the Authority's Net Pension Liability  
and Related Ratios (Presented only one year)  
(Unaudited)

Year Ended June 30, 2015  
(In thousands)

<table>
<thead>
<tr>
<th>For measurement period ended June 30, 2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Pension Liability</td>
</tr>
<tr>
<td>Service Cost</td>
</tr>
<tr>
<td>Interest on total pension liability</td>
</tr>
<tr>
<td>Difference between expected and actual experience</td>
</tr>
<tr>
<td>Changes in assumptions</td>
</tr>
<tr>
<td>Benefit Payments</td>
</tr>
<tr>
<td>Refunds of employee</td>
</tr>
<tr>
<td><strong>Net Change in total pension liability</strong></td>
</tr>
</tbody>
</table>

| Total Pension Liability - beginning         | 3,043,512 |
| Total Pension Liability - ending (a)        | $ 4,957,783 |

| Plan Fiduciary Net Position                 |
| Contributions-employer                     | $ 100,145 |
| Contributions-member                       | 36,871 |
| Net Investment Income                      | 179,151 |
| Benefit Payments                           | (216,811) |
| Administrative Expense                     | (348) |
| Refunds of Employee Contributions          | (755) |
| Transfer from other systems                | 1,274 |
| **Net Change in Plan Fiduciary Net Position** | 99,527 |

| Plan Fiduciary Net Position-beginning       | 1,299,384 |
| Plan Fiduciary Net Position-ending (b)      | $ 1,398,911 |
| Net Pension Liability-Ending (a)-(b)        | $ 3,558,872 |

| Covered-Employee Payroll                   | $ 341,910 |

| Plan Fiduciary Net Position as a percentage of the Total Pension Liability | 28.22 % |
| Net Pension Liability as a percentage of Covered-Employee Payroll          | 1.04 % |
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Notes to the Schedule of Changes in the Authority's Net Pension Liability and Related Ratios

Year Ended June 30, 2015

Benefit Changes

Benefit changes, which are reflected immediately in pension expense, can be positive, if there is a benefit improvement for existing System members, or negative if there is a benefit reduction. For the year ended June 30, 2014, there were no benefit changes to be recognized.

Changes of Assumptions

There were no changes in assumptions during the measurement year ended June 30, 2014. If there was a change in Total Pension Liability due to changes in actuarial assumption, recognition of the change would be spread over the remaining life of the System membership.
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Schedule of Employer Contributions (Unaudited)

Year Ended June 30, 2015
(In thousands)

<table>
<thead>
<tr>
<th>Fiscal Year Ended June 30</th>
<th>Actuarially Determined Employer Contribution</th>
<th>Actual Employer Contributions</th>
<th>Annual Contribution Deficiency (Excess)</th>
<th>Covered Employee Payroll</th>
<th>Actual Contributions as a percentage of Covered employee payroll</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>$100,850</td>
<td>$100,850</td>
<td>-</td>
<td>$287,143</td>
<td>34.54%</td>
</tr>
<tr>
<td>2014</td>
<td>100,145</td>
<td>100,145</td>
<td>-</td>
<td>341,910</td>
<td>29.29%</td>
</tr>
<tr>
<td>2013</td>
<td>89,481</td>
<td>89,481</td>
<td>-</td>
<td>347,094</td>
<td>25.78%</td>
</tr>
<tr>
<td>2012</td>
<td>85,361</td>
<td>85,361</td>
<td>-</td>
<td>357,758</td>
<td>23.86%</td>
</tr>
<tr>
<td>2011</td>
<td>85,313</td>
<td>85,313</td>
<td>-</td>
<td>358,458</td>
<td>23.80%</td>
</tr>
<tr>
<td>2010</td>
<td>69,926</td>
<td>69,926</td>
<td>-</td>
<td>354,955</td>
<td>19.70%</td>
</tr>
<tr>
<td>2009</td>
<td>78,490</td>
<td>78,490</td>
<td>-</td>
<td>372,344</td>
<td>21.08%</td>
</tr>
<tr>
<td>2008</td>
<td>75,768</td>
<td>75,768</td>
<td>-</td>
<td>348,361</td>
<td>21.75%</td>
</tr>
<tr>
<td>2007</td>
<td>74,343</td>
<td>74,343</td>
<td>-</td>
<td>349,028</td>
<td>21.30%</td>
</tr>
<tr>
<td>2006</td>
<td>74,513</td>
<td>74,513</td>
<td>-</td>
<td>359,272</td>
<td>20.74%</td>
</tr>
</tbody>
</table>

Notes to Schedule of Employer Contributions

Valuation Date
Actuarially determined contributions rates are calculated as of June 30, 2014, one year prior to the end of the fiscal years in which contributions are reported. Method and assumptions used to determine contribution rates for the year ended June 30, 2015 and related information for the Plan and supplemental benefits follows:

Pension Plan

- Actuarial cost method: Individual: Entry Age Normal
- Amortization method: Level percentage of pay, closed
- Remaining amortization period: 26 years
- Asset valuation method: 5-year smoothed market
- Inflation: 2.5 percent
- Salary increases: 3.5 to 7.25 percent, including inflation
- Investment rate of return: 8.25 percent, net of System investment expense, and including inflation
Supplemental Schedules
Schedules IV - VIII present certain information which is required by the 1974 Agreement. The Net Revenues data, as defined in the 1974 Agreement (Net Revenues), presented in Schedules IV and V differ in some important respects from generally accepted accounting principles (GAAP). Such differences are explained below; Schedule IV also presents a reconciliation of Net Revenues with GAAP.

The most significant differences between Net Revenues and GAAP are the following:

1. Revenues do not include investment income on investments in the construction fund (see Note 5 to the financial statements);
2. Depreciation and interest expense on bonds covered by the 1974 Agreement are not included as deductions in calculating Net Revenues;
3. Amortization of debt discount and issuance costs and the allowance for funds used during construction are not considered in the computation in calculating Net Revenues;
4. Contribution in lieu of taxes is not considered a deduction for purposes of Net Revenues;
5. Net Revenues do not include revenues or expenses of the Irrigation Systems (see Note 1 to the financial statements).

For further details and information on the definition of Net Revenues, please refer to the 1974 Agreement.
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Sources and Disposition of Net Revenues  
Under the Provisions of the 1974 Agreement  
Statements of Income (GAAP)  
and Reconciliation of Net Income  
(Unaudited)  
Year Ended June 30, 2015  
(In thousands)  

<table>
<thead>
<tr>
<th>Schedule IV</th>
<th>1974 Trust Agreement</th>
<th>2015 Statement of Income (GAAP)</th>
<th>Reconciliation of Net Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reconciliation of components of net income:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenues:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating revenues</td>
<td>$3,842,971</td>
<td>$3,865,458</td>
<td></td>
</tr>
<tr>
<td>Other operating revenues</td>
<td>31,003</td>
<td>44,263</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>(131,697)</td>
<td>(144,733)</td>
<td></td>
</tr>
<tr>
<td>1974 agreement construction fund investment income and gain on sale of other properties</td>
<td>(2,184)</td>
<td>21,404</td>
<td>$46,299</td>
</tr>
<tr>
<td>Current Expenses:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As shown</td>
<td>3,377,710</td>
<td>3,392,826</td>
<td>(15,116)</td>
</tr>
<tr>
<td>Total as defined</td>
<td>3,377,710</td>
<td>3,392,826</td>
<td></td>
</tr>
<tr>
<td>Net revenues, as defined</td>
<td>$362,383</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation</td>
<td>382,354</td>
<td>(382,354)</td>
<td></td>
</tr>
<tr>
<td>Pension expense</td>
<td>420,782</td>
<td>(420,782)</td>
<td></td>
</tr>
<tr>
<td>Other post-employment benefit (OPEB)</td>
<td>(7,358)</td>
<td>7,358</td>
<td></td>
</tr>
<tr>
<td>Disposition of Revenues:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(not classified in order of payment)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest of debt</td>
<td>$360,153</td>
<td>422,330</td>
<td></td>
</tr>
<tr>
<td>Interest on general obligation notes</td>
<td>55,084</td>
<td>55,416</td>
<td></td>
</tr>
<tr>
<td>Amortization of debt discount, financing expenses</td>
<td>-</td>
<td>(13,574)</td>
<td></td>
</tr>
<tr>
<td>Amortization of bond defeasance</td>
<td>-</td>
<td>11,595</td>
<td></td>
</tr>
<tr>
<td>Allowance for funds used during construction</td>
<td>-</td>
<td>(7,489)</td>
<td></td>
</tr>
<tr>
<td>Net interest on long-term debt</td>
<td>415,237</td>
<td>468,278</td>
<td>(53,041)</td>
</tr>
<tr>
<td>Power revenue bonds:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Principal</td>
<td>214,411</td>
<td>-</td>
<td>214,411</td>
</tr>
<tr>
<td>Appropriation capital improvements fund</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance available for Capital Improvement and other needs</td>
<td>101,250</td>
<td>-</td>
<td>101,250</td>
</tr>
<tr>
<td>Rate stabilization account</td>
<td>60,558</td>
<td>-</td>
<td>60,558</td>
</tr>
<tr>
<td>Appropriation reserve account</td>
<td>(407,346)</td>
<td>-</td>
<td>(407,346)</td>
</tr>
<tr>
<td>Contribution in lieu of taxes</td>
<td>(21,727)</td>
<td>273,460</td>
<td>(295,187)</td>
</tr>
<tr>
<td>Total expenses (GAAP)</td>
<td></td>
<td>4,930,342</td>
<td></td>
</tr>
<tr>
<td>Net revenues, as defined</td>
<td>$362,383</td>
<td></td>
<td>$(1,143,950)</td>
</tr>
<tr>
<td>Net loss</td>
<td></td>
<td>$(1,143,950)</td>
<td>$1,143,950</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  
Supplemental Schedule of Sources and Disposition  
of Net Revenues under the Provisions of the 1974 Agreement  
(Unaudited)  
Year Ended June 30, 2015  
(In thousands)  

<table>
<thead>
<tr>
<th>Schedule V</th>
</tr>
</thead>
</table>

**Sources of Net Revenues:**

**Revenues:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electric revenues</td>
<td>$3,842,971</td>
</tr>
<tr>
<td>Other operating revenues</td>
<td>31,063</td>
</tr>
<tr>
<td>Other (principally interest)</td>
<td>(133,881)</td>
</tr>
<tr>
<td><strong>Total Revenues</strong></td>
<td><strong>3,740,093</strong></td>
</tr>
</tbody>
</table>

**Current Expenses:**

**Operations:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fuel</td>
<td>1,887,245</td>
</tr>
<tr>
<td>Purchased Power</td>
<td>789,717</td>
</tr>
<tr>
<td>Other production</td>
<td>53,495</td>
</tr>
<tr>
<td>Transmission and distribution</td>
<td>145,468</td>
</tr>
<tr>
<td>Customer accounting and collections</td>
<td>98,852</td>
</tr>
<tr>
<td>Administrative and general</td>
<td>236,557</td>
</tr>
<tr>
<td>Maintenance</td>
<td>166,395</td>
</tr>
<tr>
<td><strong>Total Current Expenses</strong></td>
<td><strong>3,377,769</strong></td>
</tr>
</tbody>
</table>

**Net revenues, as defined**

$362,384

**Disposition of Net Revenues:**

**Revenue fund:**

Power revenue bonds - sinking fund requirements:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest</td>
<td>$360,153</td>
</tr>
<tr>
<td>Principal</td>
<td>214,411</td>
</tr>
<tr>
<td>Reserve Account</td>
<td>(407,346)</td>
</tr>
<tr>
<td>Rate Stabilization Account</td>
<td>60,558</td>
</tr>
<tr>
<td>Balance available for Capital Improvement and other needs</td>
<td>101,250</td>
</tr>
<tr>
<td><strong>Total Revenue Fund</strong></td>
<td><strong>329,026</strong></td>
</tr>
</tbody>
</table>

**General obligation notes:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest</td>
<td>55,084</td>
</tr>
<tr>
<td><strong>Total General Obligation Notes</strong></td>
<td><strong>(21,722)</strong></td>
</tr>
</tbody>
</table>

**Net revenues, as defined**

$362,383
## Schedule VI

### By Account:

<table>
<thead>
<tr>
<th>Account Description</th>
<th>Held by Authority</th>
<th>Restricted Deposits with Trustee</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
<td>Other Assets</td>
</tr>
<tr>
<td>1974 Agreement (restricted)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sinking Fund - Bond Services</td>
<td>$5,098</td>
<td>$2,409</td>
</tr>
<tr>
<td>Reserve Account</td>
<td>236,787</td>
<td>236,787</td>
</tr>
<tr>
<td>Self-Insurance Fund</td>
<td>100,152</td>
<td>100,152</td>
</tr>
<tr>
<td>Sinking Fund - Capitalized Interest</td>
<td>48,744</td>
<td>48,744</td>
</tr>
<tr>
<td>Reserve Maintenance Fund</td>
<td>16,040</td>
<td>16,040</td>
</tr>
<tr>
<td>Other Restricted Fund</td>
<td>1,929</td>
<td>1,929</td>
</tr>
<tr>
<td>Construction Fund:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rural Utilities Services (RUS)</td>
<td>1,106</td>
<td>1,106</td>
</tr>
<tr>
<td>Other</td>
<td>133,966</td>
<td>133,966</td>
</tr>
<tr>
<td>PREPA Client Fund</td>
<td>3,180</td>
<td>3,180</td>
</tr>
<tr>
<td>General purpose (unrestricted)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General (excluding Prepa act)</td>
<td>244,663</td>
<td>244,663</td>
</tr>
<tr>
<td>Working funds</td>
<td>9,663</td>
<td>9,663</td>
</tr>
<tr>
<td>Total</td>
<td>$801,328</td>
<td>$410,547</td>
</tr>
</tbody>
</table>

### By Type of Assets Held:

<table>
<thead>
<tr>
<th>Asset Type</th>
<th>Held by Authority</th>
<th>Restricted Deposits with Trustee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Working funds</td>
<td>$399</td>
<td>$399</td>
</tr>
<tr>
<td>PREPA Client Fund</td>
<td>3,180</td>
<td>3,180</td>
</tr>
<tr>
<td>Cash in bank and time deposits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(by depository institutions)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government Development bank for Puerto Rico</td>
<td>139,000</td>
<td>139,000</td>
</tr>
<tr>
<td>Banco Popular de Puerto Rico</td>
<td>26,315</td>
<td>26,315</td>
</tr>
<tr>
<td>Citibank, N.A.</td>
<td>197,730</td>
<td>197,730</td>
</tr>
<tr>
<td>US Bank</td>
<td>65</td>
<td>65</td>
</tr>
<tr>
<td>US Bank - Service Bond</td>
<td>5,098</td>
<td>5,098</td>
</tr>
<tr>
<td>Oriental Bank</td>
<td>8,134</td>
<td>8,134</td>
</tr>
<tr>
<td>First Bank, San Juan, Puerto Rico</td>
<td>78</td>
<td>78</td>
</tr>
<tr>
<td>Banco Santander, San Juan, Puerto Rico</td>
<td>17,665</td>
<td>17,665</td>
</tr>
<tr>
<td>Scotiabank</td>
<td>23</td>
<td>23</td>
</tr>
<tr>
<td>Investment Securities</td>
<td>404,846</td>
<td>17,958</td>
</tr>
<tr>
<td>Total</td>
<td>$801,328</td>
<td>$410,547</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Supplemental Schedule of Changes in Cash and Investments by Funds  

Year Ended June 30, 2015  
(In thousands)  

Schedule VII  

<table>
<thead>
<tr>
<th>2014-15 Activity</th>
<th>General Purpose Fund</th>
<th>Reserve for Current Expenses Fund</th>
<th>Sinking Fund</th>
<th>Other Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual net revenue from operations:</td>
<td>-</td>
<td>(362,281)</td>
<td>(21,727)</td>
<td>-</td>
</tr>
<tr>
<td>Funds provided from internal operations</td>
<td>275,053</td>
<td>275,053</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1974 Agreement Investment Income Act 4191 Investment income and other</td>
<td>(2,184)</td>
<td>(2,184)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Unrealized gain (loss) on market value of investments</td>
<td>20,804</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Offsets of current years contribution in lieu of taxes against certain government accounts receivable</td>
<td>3,110</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Offsets of current years 95% contributions in lieu of taxes against Commonwealth of Puerto Rico transfers to General Obligations</td>
<td>-</td>
<td>39,228</td>
<td>(39,228)</td>
<td>-</td>
</tr>
<tr>
<td>Proceeds from contributed capital</td>
<td>-</td>
<td>10,365</td>
<td>(10,365)</td>
<td>-</td>
</tr>
<tr>
<td>Proceeds used for construction (191,500)</td>
<td>10,419</td>
<td>10,419</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Proceeds from Federal Agencies and Insurance Companies</td>
<td>14,972</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Financing</td>
<td>1,479</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Proceeds from Notes Payables</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Continues
Puerto Rico Electric Power Authority  
(A Component Unit of the Commonwealth of Puerto Rico)  

Supplemental Schedule of Changes in Cash and Investments by Funds  

Year Ended June 30, 2015  
(In thousands)  

Schedule VII

<table>
<thead>
<tr>
<th>2014-15 Activity</th>
<th>General Fund</th>
<th>Sinking Fund</th>
<th>Other Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deteriorated bonds-net of original discounts</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Sinking Funds and account transfers</td>
<td>-</td>
<td>43,177</td>
<td>-</td>
</tr>
<tr>
<td>Notes issued to working capital</td>
<td>11,566</td>
<td>11,566</td>
<td>-</td>
</tr>
<tr>
<td>Note issued to finance the acquisition of fuel oil</td>
<td>156,874</td>
<td>156,874</td>
<td>-</td>
</tr>
<tr>
<td>Payment of notes payable</td>
<td>(156,929)</td>
<td>(156,929)</td>
<td>-</td>
</tr>
<tr>
<td>Payment of interest</td>
<td>(484,284)</td>
<td>(56,799)</td>
<td>-</td>
</tr>
<tr>
<td>Expenses on investment</td>
<td>179</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Payment of current maturities of long-term debt</td>
<td>(204,305)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Working funds</td>
<td>8,664</td>
<td>(21)</td>
<td>-</td>
</tr>
<tr>
<td>Accounts receivable (includes non-current)</td>
<td>(360,141)</td>
<td>(360,141)</td>
<td>-</td>
</tr>
<tr>
<td>Fuel oil</td>
<td>130,338</td>
<td>130,338</td>
<td>-</td>
</tr>
<tr>
<td>Materials and supplies</td>
<td>1,982</td>
<td>1,982</td>
<td>-</td>
</tr>
<tr>
<td>Prepayments and other</td>
<td>(1,465)</td>
<td>(1,465)</td>
<td>-</td>
</tr>
<tr>
<td>Other assets</td>
<td>(11,707)</td>
<td>(11,707)</td>
<td>-</td>
</tr>
<tr>
<td>Deferred outflows of resources</td>
<td>(1,452,442)</td>
<td>(1,452,442)</td>
<td>-</td>
</tr>
<tr>
<td>Deferred inflows of resources</td>
<td>57,703</td>
<td>57,703</td>
<td>-</td>
</tr>
<tr>
<td>Net pension liability</td>
<td>814,744</td>
<td>814,744</td>
<td>-</td>
</tr>
<tr>
<td>Accounts payable and accrued liabilities (includes non-current)</td>
<td>(283,922)</td>
<td>(283,922)</td>
<td>-</td>
</tr>
<tr>
<td>Customer deposits</td>
<td>1,343</td>
<td>1,343</td>
<td>-</td>
</tr>
<tr>
<td>Adjustments</td>
<td>(43,312)</td>
<td>53,982</td>
<td>71,317</td>
</tr>
<tr>
<td>Total before interfund accounts</td>
<td>501,328</td>
<td>333,758</td>
<td>11</td>
</tr>
<tr>
<td>Add (deduct) Interfund Accounts</td>
<td>-</td>
<td>(333,556)</td>
<td>-</td>
</tr>
<tr>
<td>Balance at June 30, 2015</td>
<td>$501,328</td>
<td>$2</td>
<td>$11</td>
</tr>
</tbody>
</table>
Puerto Rico Electric Power Authority
(A Component Unit of the Commonwealth of Puerto Rico)

Supplemental Schedule of Changes in Long-Term Debt and Current Portion of Long-Term Debt
(Unaudited)
Year Ended June 30, 2015
(In thousands)

Schedule VIII

Long-term debt, excluding current portion:

Balance at beginning of year $8,247,066
Transfers to current liabilities:
Power revenue bonds (236,472)
Notes payable 56
Payment of general obligation notes:
Notes payable (158,888)
Remainder 7,851,702

New issues:
Power revenue bonds -
Power revenue refunding bonds -
Debt discount on new bond issues - net -
Defeasance of bonds -
Debt discount on cancelled bonds - net -
Notes payable 168,440
Balance at end of year $8,020,142

Current portion of long-term debt:

Balance at beginning of year $1,166,189
Transfer from long-term debt 236,416
Payments to bondholders:
Power revenue - July 1 (204,365)
Amortization of debt discount (15,154)
Balance at end of year $1,183,106
Report on Internal Control
Report of Independent Auditors 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

The Board of Directors
Puerto Rico Electric Power Authority

We have audited, in accordance with auditing standards generally accepted in the United States 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 Electric Power Authority (the Authority), which comprise the statement of net position as of June 30, 2015, and the related statements of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated April 20, 2018. Our report includes a reference to other auditors who audited the financial statements of PREPA Holdings LLC as described in our report on the Puerto Rico Electric Power Authority’s financial statements. This report does not include the results of the other auditors’ testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. We expressed a qualified opinion on the financial statements based on the circumstances noted in our report.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or 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 have not been identified. We consider the deficiencies described in the accompanying Schedule of Findings and Responses as items 2015-001 through 2015-003 to be material weaknesses.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Authority’s financial statements are free of 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 Authority’s Response to Findings**

The Authority’s response to the findings identified in our audit are described in the Schedule of Findings and Responses. The Authority’s response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result 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.

April 20, 2018

Stamp No. E318303
affixed to
original of
this report.