



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

March 22, 2017

**Puerto Rico National Guard  
Administration  
San Juan, Puerto Rico**

In connection with our audit of the basic financial statements of the **Puerto Rico National Guard (the PRNG)** as of and for the year ended June 30, 2016, we considered its internal control structure in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control structure.

Also, as part of obtaining reasonable assurance about whether the basic financial statements are free of material misstatements, we performed test over the PRNG's compliance with certain provisions of laws, regulations, contracts and grants. However, the objective of our audit of the financial statements was not to provide an opinion or overall compliance with such provisions.

As a result of our evaluation, we noted certain areas where financial matters should be considered, procedures improved and administrative controls strengthened. This memorandum summarizes our comments and suggestions. These comments are not significant enough to be considered significant deficiencies as defined by AU Section 325 "*Communicating Internal Control Related Matters Identified in an Audit*". A separate report dated March 22, 2017 contains our report on the **PRNG's** internal control structure, and separate report dated March 22, 2017 contain our report on compliance with laws, regulations, contracts, and grants based on an audit of the financial statements. This letter does not affect our report dated March 22, 2017 on the financial statements as of and for the year ended June 30, 2016.

We hope to provide our services to you in the next fiscal year audit. Thank you for your trust in our Firm.

Cordially,

  
Ángel Alfredo López Vega, CPA  
President

López-Vega, CPA, PSC

**A. Accrued Vacation and Sick Leave**

We performed a test over a sample of 40 employees' files and payroll transactions. As a result of our test, we noted some differences in the vacation or sick leave days balance reported in the accrued vacation and sick leave report as of June 30, 2016 and the time cards details of the employee.

**Recommendation**

Accrued vacation and sick leave report should be reconciled on a monthly basis accordingly to the time detail card of the employees. Proper monitoring procedures should be followed by the **PRNG's** Human Resources Department.

**B. Reimbursements Requests**

We examined a sample of 18 reimbursements requests submitted to the federal agency. We verified if the costs for which reimbursement was requested, were paid prior to the date of the request. As a result of our test, we noted that costs were paid prior to the reimbursements requests as required. However, for some costs reimbursement requested, the time elapsed between the disbursement and the request submitted by the **PRNG** to the federal agency, took several days or months. As management states, the financial condition and liquidity of the Commonwealth of Puerto Rico and the Government Development Bank has deteriorated. As a result, payments issued for goods and services providers has been held by the Treasury Department of Puerto Rico and reimbursement vouchers are prepared when they are finally delivered.

**Recommendation**

Management should continue to strength its internal control procedures related to the processing and submission of reimbursements request in coordination with the Treasury Department of Puerto Rico. The agency shall submit the requests in a reasonable time frame after the disbursements are issued, in order to improve cash flow and manage the funds to cover operational costs.



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**NATIONAL GUARD OF THE  
COMMONWEALTH OF PUERTO RICO**

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**BASIC FINANCIAL STATEMENTS – CASH  
BASIS, REQUIRED SUPPLEMENTARY  
INFORMATION AND INDEPENDENT AUDITORS'  
REPORT (WITH ADDITIONAL REPORTS  
REQUIRED BY THE SINGLE AUDIT ACT)**

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**For the Year Ended June 30, 2016**

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## **INDEPENDENT AUDITORS' REPORT**

**National Guard of the  
Commonwealth of Puerto Rico  
San Juan, Puerto Rico**

### **Report on the Financial Statement**

We have audited the accompanying financial statements – cash basis of the governmental activities, each major fund, and the aggregated remaining fund information arising from the cash transactions of the **National Guard of the Commonwealth of Puerto Rico (the PRNG)** as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the **PRNG's** basic financial statements as listed in the table of contents.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the cash basis of accounting described in **Note 1**; this includes determining that the cash basis of accounting is acceptable basis for the preparation of the financial statements in these circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 audit opinion.



## INDEPENDENT AUDITORS' REPORT (CONTINUED)

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the receipts and disbursements of the governmental activities, each major fund, and the aggregate remaining fund information of the **PRNG** for the year ended June 30, 2016, in conformity with the basis of accounting described in **Note 1**.

### **Basis of Accounting**

As described in **Note 1**, the **PRNG** prepares its basic financial statements on the basis of cash receipts and cash disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Also, as described in **Note 1**, the financial statements of the **PRNG** are intended to present the cash receipts and cash disbursements of only that portion of the financial reporting entity of the Commonwealth of Puerto Rico that is attributable to the transactions of the **PRNG**.

### **Other Matters**

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages **4** through **11** and **24** be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with the auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

#### *Other Information*

Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the **PRNG's** basic financial statements. The accompanying schedule of expenditures of federal awards on page **26** is presented for purposes of additional analysis as required by Title 2 U.S. Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Costs Principles, and Audit Requirements for Federal Awards and is 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 statement of receipts and disbursements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the statement of receipts and disbursements or to the statement of receipts and disbursements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America.





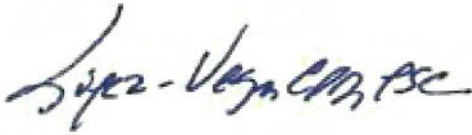
**INDEPENDENT AUDITORS' REPORT (CONTINUED)**

*Other Information (Continued)*

In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

**Other Reporting Required by Government Auditing Standards**

In accordance with Government Auditing Standards, we have also issued our report dated March 22, 2017, on our consideration of **PRNG's** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering **PRNG's** internal control over financial reporting and compliance.



LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico  
March 22, 2017

Stamp No. 2728539 of the Puerto Rico  
Society of Certified Public Accountants  
was affixed to the record copy of this report.



*López-Vega, CPA, PSC*

Certified Public Accountants / Management Advisors

## INTRODUCTION

As management of the **National Guard of the Commonwealth of Puerto Rico (PRNG)**, we offer to the readers of this annual financial report our discussion and analysis of the **PRNG's** financial performance during the fiscal year ended June 30, 2016. The following discussion and analysis has been designed to accomplish the following goals:

- Assist the reader in focusing on significant financial issues;
- Provide an overview of the **PRNG's** financial activity;
- Identify any material deviations from the financial plan (the approved budget), and;
- Identify individual fund issues or concerns.

Since the MD&A is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the **PRNG's** financial statements.

## ORGANIZATION AND MISSION STATEMENT

The **PRNG** was created by Law No. 62 of June 23, 1969. The purpose of the **PRNG** is to protect lives and property, preserve the peace, public order and safety during emergency situations as a result of natural disasters and civil uproar, and serve as national security corps whenever Congress may declare a state of emergency situation when it becomes part of the U.S. Army.

The **PRNG** maintains 48 armories, and is present in 30 communities. The Puerto Rico National Guard, like the National Guards in all 50 states, is a hybrid organization. National Guards are ordinarily under the control of state (or, in the case of Puerto Rico, Commonwealth) officials, but are organized pursuant to federal statute, and in war time or other emergencies, Guard units may be brought under federal control. The Puerto Rico Army National Guard and Reserve units support U.S. Army South's (USARSO) many multilateral exercises and programs. It is through this integration of our Active Army, National Guard, and Reserves that USARSO can maximize resources to carry out missions.

The **PRNG** is headed by an Adjutant General appointed by the Governor of Puerto Rico. Also, the **PRNG** has the following programs:

**General Management and Administration:** Coordinates General Assistant's Office, Military Personnel Division, Legal Services, Public Relations, and Human Resources offices. It directs and supervises military troops.

The purpose of the program is to direct, coordinate, and effectively supervise the operations and services offered by the Puerto Rico National Guard, at State and Federal level, with the U.S. Army Reserve. It maintains operations and services of the P.R. National Guard. Its objective is to correctly administer the appropriated resources and maintain the troops' efficiency rate by means of training in and outside of Puerto Rico.

**Puerto Rico State Guard:** Professional Officers of the Corps of Volunteers that offer security support and medical services. The Puerto Rico State Guard is commanded by a Brigadier General and is composed by four brigades established in the Metropolitan Area, Ponce, Mayagüez and Caguas.



## ORGANIZATION AND MISSION STATEMENT (CONTINUED)

The purpose of the program is to be activated and offer support to the P.R. National Guard on a moment's notice, when activated by the Governor of Puerto Rico and the President of the United States. Its goal is to provide representation of the Puerto Rico National Guard in civic activities, assist the National Guard in emergency cases, offering support and medical services to the community. In addition, they furnish administrative support to the different entities of the Agency.

**Security and Preservation of Military Facilities:** Provides security services to different military facilities throughout the Island, with the purpose of preserving law and order to protect lives and properties. It includes the operation and preservation of the National Guard's physical facilities. These tasks are accomplished with state resources and, in some cases, by means of agreements with the Federal National Guard Bureau.

The program's purpose is to uphold security in military installations as well as maintain their physical facilities. Its goal is to protect the military quarters and facilities of the National Guard of Puerto Rico.

**Administration Auxiliary Services:** Renders administrative services to the Administrative Services Division, including Finance, Budget and General Services; whether state and/or Federal appropriations.

The purpose of the program is to maximize assigned resources, prepare a monthly budget, control and maintain property inventory, develop the Mechanization Plan and provide necessary services required by the different military installations. Its goal is to manage the Agency's fiscal resources to ensure they comply with established laws. In addition, one of its objectives is to complete the Mechanization Plan so as to improve and update information systems.

### • FINANCIAL HIGHLIGHTS

- In the **PRNG's** Statement of Activities – Governmental Activities, the actual cash receipts exceeded actual cash disbursements by \$1,056,172, resulting in a decrease of \$3,449,782 compared with prior fiscal year (\$4,505,954).
- In the Combined Statement of Cash Receipts and Cash Disbursements – Governmental Funds, Cash Receipts decreased by \$2,701,521 and cash disbursements increased by \$748,261 when compared to prior year financial statements.
- The General Fund (the primary operating fund) reflected \$1,359,662 in cash receipts over cash disbursements. However, the Federal Fund and Other Governmental Funds reflected cash disbursements over cash receipts amounting to \$193,821 and \$109,669, respectively.
- On a budgetary basis, actual cash receipts and disbursements amounted to \$9,659,000.

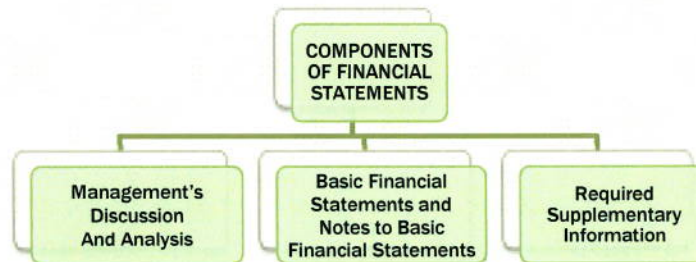


## BASIC FINANCIAL STATEMENTS PRESENTATION

The approach used in the presentation of the financial statements of the **PRNG** is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2015-2016. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance.

### Overview of the Financial Statements

The **PRNG's** basic financial statements comprise three components: (1) management's discussion and analysis, (2) basic financial statements, and (3) required supplementary information.



- **Basic Financial Statements** -The **PRNG** uses the cash basis of accounting to account for all funds administered. Under this method, revenue received is recognized as cash when funds are transferred – in and expenditures are recognized when funds are disbursed or transferred – out. Therefore, the statements are not intended to present the **PRNG's** results of operations in accordance with accounting principles generally accepted in the United States of America.

The Statement of Activities is presented in the cash basis of accounting, which presents the cash receipts and cash disbursements of only that portion of the financial reporting entity of the Commonwealth of Puerto Rico that is attributable to the transactions of the **PRNG**. The Financial Statements also includes notes to the Statement of Activities – Cash Basis section that explains some information in the financial statements and provides more detailed data.

The Combined Statement of Cash Receipts and Cash Disbursements for All Governmental Funds provides detailed information about the **PRNG's** most significant funds, not the **PRNG** as a whole.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government - Wide Financial Statements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the **PRNG's** near term financial decisions.

**Overview of the Financial Statements (Continued)**

- **Notes to the Financial Statements** – Provides integral information needed to explain the basis for the financial information reported on the Basic Financial Statements and more detailed data for its further analysis.
- **Required Supplementary information** – Provides additional information to better understand the financial position of the **PRNG** and contains the Budgetary Comparison Schedule for the General Fund.

**FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE**

**Statement of Activities**

The **PRNG's** total cash receipts decreased by \$2,701,521, representing a decrease of 7.45% compared to prior year's financial statements. During the fiscal year ended June 30, 2016, 32.74% of **PRNG's** total cash receipts came from state-general fund assignments, while 67.26% resulted from federal grants. The **PRNG's** disbursements cover a range of services. The following table includes a comparative analysis for readers to have comparative information with the percentage of change in cash receipts and disbursements from prior year to current year.

Statements of Activities	2016	2015	Change	%
Program cash receipts:				
Legislative appropriations	\$ 10,988,000	\$ 13,309,250	\$ (2,321,250)	(17.44)%
Federal programs	22,575,704	22,955,975	(380,271)	(1.66)%
<b>Total cash receipts</b>	<b>33,563,704</b>	<b>36,265,225</b>	<b>(2,701,521)</b>	<b>(7.45)%</b>
Program cash disbursements:				
Administration and direction	1,051,214	994,079	57,135	5.75%
Security and conservation of military facilities	6,421,890	6,730,600	(308,710)	(4.59)%
State Guard	1,810	73,997	(72,187)	(97.55)%
Auxiliary services of administration	824,424	1,018,377	(193,953)	(19.05)%
Special programs	1,438,669	856,926	581,743	67.89%
Public security activities	22,769,525	22,085,292	684,233	3.10%
<b>Total cash disbursements</b>	<b>32,507,532</b>	<b>31,759,271</b>	<b>748,261</b>	<b>2.36%</b>
Excess of cash receipts over cash disbursements	\$ 1,056,172	\$ 4,505,954	\$ (3,449,782)	(76.56)%



**FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE (Continued)**

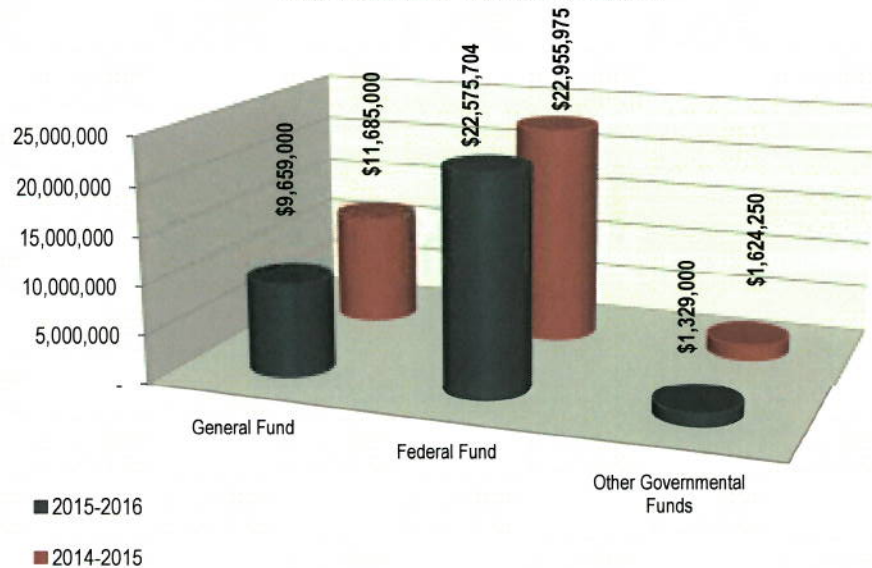
**Governmental Fund Financial Statements**

The governmental fund financial statements focus on major funds. The **PRNG's** major funds are the general fund (which accounts for the main operating activities of the **PRNG**), federal fund (which account for all grants received from federal programs) and other governmental funds (which account for other legislative resolutions, fees and charges for services and other income). The **PRNG's** Combined Statement of Cash Receipts and Cash Disbursements for fiscal year ended June 30, 2016, presented those three major funds.

The following figures provide information about how the governmental entity financed its activities and distributed the resources during the last two years.

Figure 1  
**CASH RECEIPTS COMPARISON**

**FIGURE 1** presents cash receipts comparison during the last two years



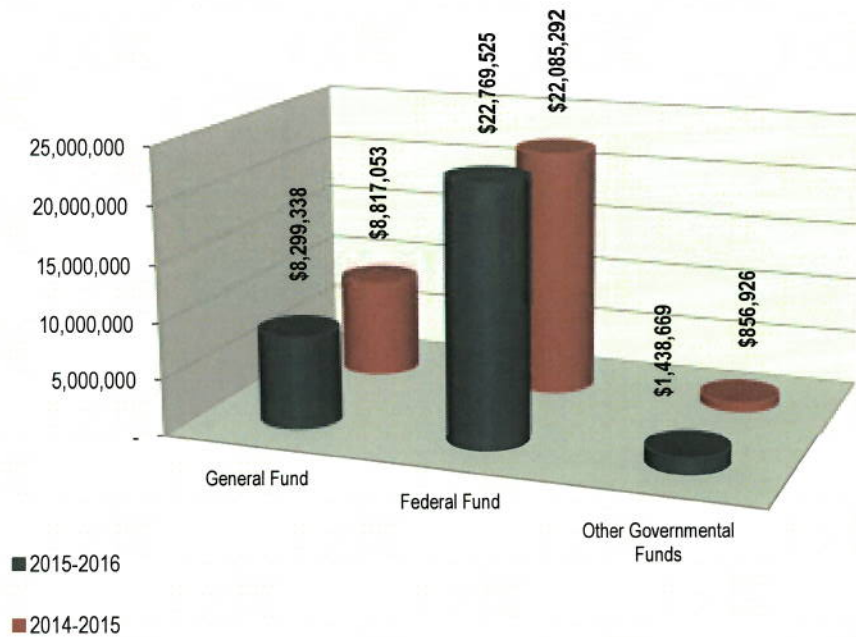


FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE (Continued)

Figure 2

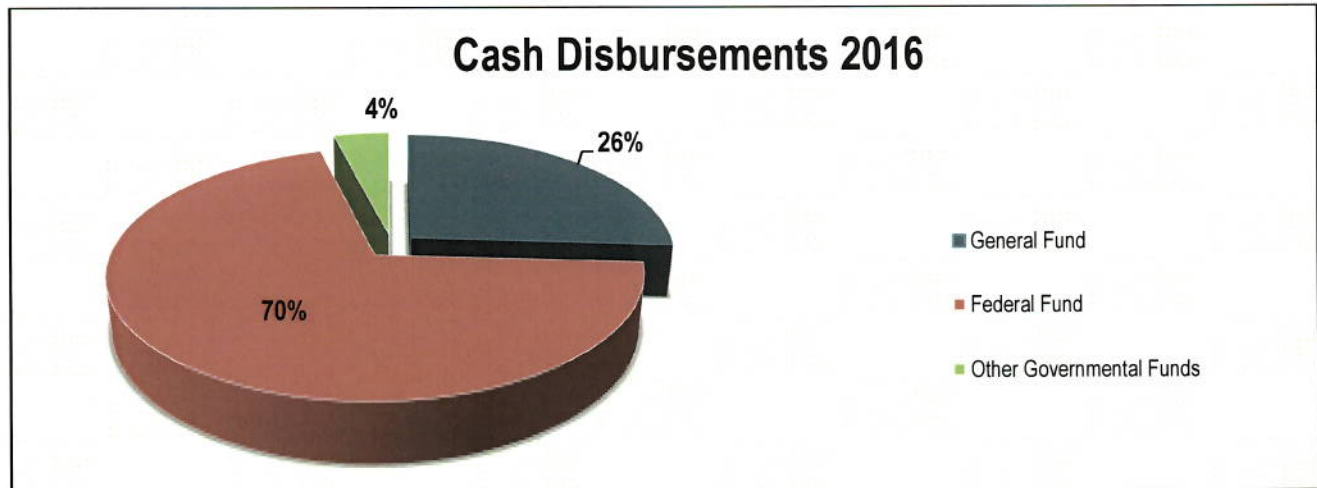
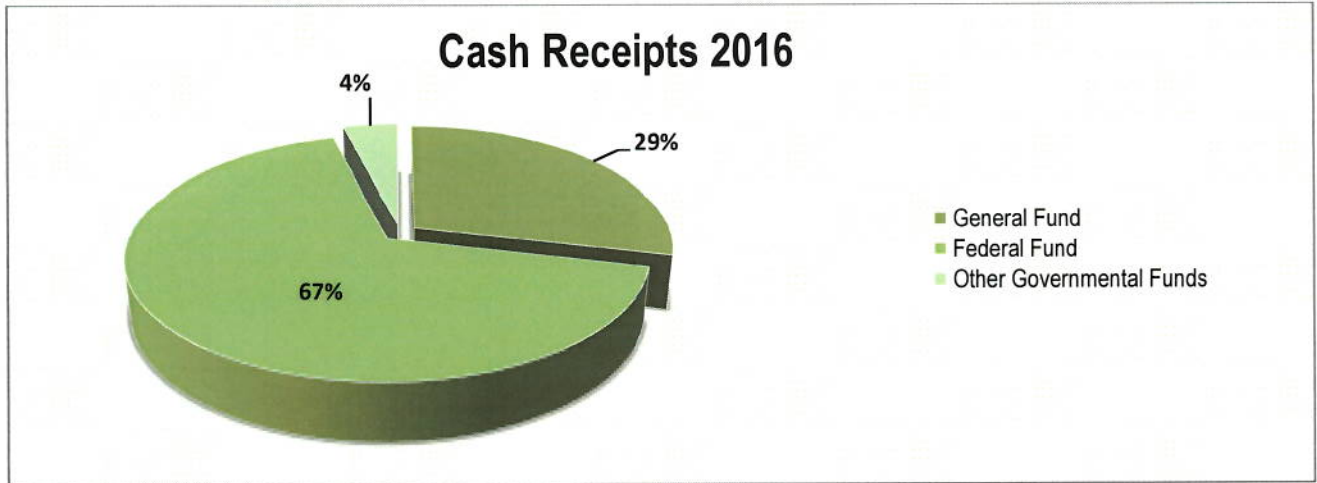
CASH DISBURSEMENTS COMPARISON

FIGURE 2 presents cash disbursements comparison during the past two years



The following figures present how governmental activities of the **PRNG's** basic services were financed and distributed. These activities are primarily financed through state assignments, federal grants, charges for services and other revenues. The accounts of the **PRNG** are organized on three fund types: general fund, federal fund and other governmental funds. The **PRNG** maintains appropriations for various individual state and federal funds within each fund type. The state appropriations are presented as general fund and other governmental funds, which correspond to the funds accounted for the operations of the **PRNG** and appropriations granted for specific purposes, respectively. The measurement focus of the **PRNG's** governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending and determination of the excess (deficiency) of receipts over (under) cash disbursements, rather than upon net income determination. Such financial information is useful in assessing the **PRNG's** financing requirements.

FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE (Continued)





## GENERAL FUND BUDGETARY HIGHLIGHTS

A budget is prepared for the General Fund and represents legislative appropriations for the general operation of the **PRNG**. The procedures followed for approval and operations of the budget are defined by the laws of Commonwealth of Puerto Rico. The approved budget for fiscal year 2015-2016 amounted to \$9,659,000. On a budgetary basis, actual cash receipts and disbursements amounted to \$9,659,000.

## ECONOMIC FACTORS

The Commonwealth of Puerto Rico (the Commonwealth) and its instrumentalities are currently facing a severe fiscal and liquidity crisis. This is the culmination of many years of significant governmental deficits, a prolonged economic recession (which commenced in 2006), high unemployment, population decline, and high levels of debt and pension obligations. Also, credit rating agencies have been downgrading their ratings on the Commonwealth debt obligations based on, among other problems, years of deficit financing, pension underfunding, budgetary imbalance, and as mentioned before, years of prolonged recession.

As more fully explained in Note 7 to the financial statements, the Governments of the United States of America and the Commonwealth of Puerto Rico have approved and implemented certain laws to overcome this crisis. Following are some of the measurements implemented to this end:

- **Puerto Rico Fiscal and Economic Growth Plan** - On September 9, 2015, the Working Group for the Fiscal and Economic Recovery of Puerto Rico established by the Governor Alejandro García Padilla by executive order EO 2015-022 submitted the Fiscal and Economic Growth Plan (FEGP), setting forth economic development, structural, fiscal and institutional reform measures intended to meaningfully reduce the Commonwealth's projected financing gaps.
- **Puerto Rico Emergency Moratorium and Financial Rehabilitation Act** - On April 6, 2016, the Legislature approved Act No. 21, known as the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act (the Act). This Act empowers the Governor with narrowly tailored authority within the boundaries of the Commonwealth's laws and Constitution, to enable the Commonwealth and its instrumentalities to continue providing essential services to Puerto Rico's residents while addressing the critical need for structural and fiscal reform and debt.
- **Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA)** - On June 30, 2016, the U.S. President signed the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), which grants the Commonwealth and its component units access to an orderly mechanism to restructure their debts in exchange for significant federal oversight over the Commonwealth's finances.

## FINANCIAL CONTACT

The **PRNG's** financial statements are designed to present the readers with a general overview of the cash receipts and cash disbursements of the **PRNG**. Questions or concerns regarding any information in this report or requests for additional information should be addressed to the National Guard of the Commonwealth of Puerto Rico, General Esteves St. #100, San Juan, P.R. 00901.



**Program cash disbursements:**

Administration and direction	\$ 1,051,214
Security and conservation of military facilities	6,421,890
State Guard	1,810
Auxiliary services of administration	824,424
Special programs	1,438,669
Public security activities	<u>22,769,525</u>
Total program cash disbursements	<u>32,507,532</u>

**Program cash receipts:**

Legislature appropriations	10,988,000
Federal programs	<u>22,575,704</u>
Total program cash receipts	<u>33,563,704</u>

<b>Excess of cash receipts over cash disbursements</b>	<u>\$ 1,056,172</u>
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See accompanying notes to basic financial statements – cash basis.

	General Fund	Federal Fund	Other Governmental Funds	Total
<b>Cash receipts:</b>				
Legislative appropriations	\$ 9,659,000	-	\$ 1,329,000	\$ 10,988,000
Federal appropriation	-	22,575,704	-	22,575,704
Total cash receipts	<u>9,659,000</u>	<u>22,575,704</u>	<u>1,329,000</u>	<u>33,563,704</u>
<b>Cash disbursements:</b>				
Administration and direction	1,051,214	-	-	1,051,214
Security and conservation of military facilities	6,421,890	-	-	6,421,890
State Guard	1,810	-	-	1,810
Auxiliary services of administration	824,424	-	-	824,424
Special programs	-	-	1,438,669	1,438,669
Public security activities	-	22,769,525	-	22,769,525
Total cash disbursements	<u>8,299,338</u>	<u>22,769,525</u>	<u>1,438,669</u>	<u>32,507,532</u>
Excess of cash receipts over cash disbursements	<u>\$ 1,359,662</u>	<u>\$ (193,821)</u>	<u>\$ (109,669)</u>	<u>\$ 1,056,172</u>

See accompanying notes to basic financial statements – cash basis.

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:**

**Organization**

The **National Guard of the Commonwealth of Puerto Rico (PRNG)** was created by the Law No. 28 of 1917, which was subsequently amended by Law No. 62 of June 23, 1969, as amended. The Law established the **PRNG** as the duly authorized governmental agency to protect the lives and properties of the Puerto Rico residents, to preserve the peace, the order and the public security in emergency situations caused by natural disasters or public riots. The **PRNG** maintains 48 armories, and is present in 30 communities. The **PRNG**, like the National Guards in all 50 states of the United States of America, is a hybrid organization. National Guards are ordinarily under the control of the State (or, in the case of Puerto Rico, of the Commonwealth) officials, but are organized pursuant to federal statute, and in war time or other emergencies, guard units may be brought under Federal control. The Puerto Rico National Guard and Reserve units support the U.S. Army South's (South COM) many multilateral exercises and programs. It is through this integration of the U.S.A. Active Army, National Guard, and Reserves that South COM can maximize resources to carry out missions.

As part of its programs, the **PRNG** established the Youth Programs to provide a highly disciplined atmosphere fostering academics, leadership development, physical training, and personal growth to educate and train unemployed high school dropout youths and make them productive members of the community. The **PRNG** also supports communities using their specialized skills. Medical units provide preventive health care, education, and immunizations in low-income neighborhoods. Guard members serve drug and law enforcement agencies through its Counter Drug program, resulting in the confiscation of millions of dollars in illegal drugs. The **PRNG** conducts two National Guard Bureau sponsored youth programs: STARBASE and Challenge.

**Financial reporting entity**

The **PRNG** is for financial reporting purposes, part of the Commonwealth of Puerto Rico; its financial data is included as part of the Commonwealth of Puerto Rico's financial statements, and as such, the Department of the Treasury of the Commonwealth of Puerto Rico serves as trustee of the funds assigned to the **PRNG** by the Legislative Branch and Federal Agencies. The Treasury Department also handles and records expenditures made with such funds and provides the **PRNG** with reports regarding such activities.

The financial information included in the accompanying Combined Statement of Cash Receipts and Cash Disbursements was obtained from the Puerto Rico Treasury Department's Integrated Financial Accounting System (PRIFAS) and is issued solely to comply with the Single Audit Act of 1984, P.L. 98-502, and the Single Audit Act Amendments of 1986, P.L. 104-156 and for the information to the federal awarding agencies, pass-through entities, regulators, management and those charged with the governance.



## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Basis of presentation

The accounts of the **PRNG** are organized on the basis of the three fund types: general fund, federal fund, and others governmental funds. The **PRNG** maintains appropriations for several individual state and federal funds within each fund type. Those state appropriations are presented as general fund and other governmental funds, which correspond to the funds accounted for the **PRNG** and appropriations granted for specific purposes, respectively. As more fully explained in the section "Basis of Accounting" below, each fund is accounted for with a set of accounts which include only receipts and disbursements. No balance sheet accounts are reported. The individual funds account for the governmental resources allocated to them for purposes of carrying on specific activities in accordance with laws, regulations and other restrictions. State funds are appropriated by the Legislature of the Commonwealth of Puerto Rico and are funds through which most functions typically are financed. Federal funds reflect the federal financial assistance managed by the **PRNG** from programs funded by the Federal Government. The individual funds included in these fund types are classified accordance with their cost category.

The following governmental fund types are used by the **PRNG**:

**General Fund** – The general fund is the primary operating fund of the **PRNG**. It is used to account for all financial resources, except those required to be accounted for in another fund. The current financial resources accounted for in this fund consist of legislative appropriations approved by the Commonwealth of Puerto Rico. The general fund is divided in the following programs:

**Management and Administration** – This program is used to account for resources and expenditures related to the supervision and coordination of all services and operation of the National Guard of Puerto Rico.

**Security and Military Facilities Maintenance** – This program is used to account for resources and expenditures related to the security of military installations, as well as the operation and maintenance of their physical facilities. This program uses state resources and in some cases federal funds through service agreements with the Federal National Guard section.

**State Guard** – This program is used to account for resources and expenditures related to the security, protection and health services of Puerto Rico, especially in those cases in which the Governor of Puerto Rico activates the State Guard.

**Auxiliary Services of Administration** – This program is used to account for resources and expenditures related to auxiliary activities and complementary service of all the offices and programs that use state funds and federal services agreements for its operation.

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Basis of presentation (continued)

**Federal Fund** – This fund is used to account for specific revenue sources that are legally restricted to cover disbursements for specific purposes in accordance with federal regulations. The resources and expenditures accounted for in this fund include the proceeds received from the USA Department of Defense to support the operation and maintenance of the National Guard facilities.

In addition, this fund accounts for the Starbase and Challenge youth programs.

**Other Governmental Funds** – This fund is used to account for resources of funds that are deposited for specific purposes with applicable laws. They may come from service fees, donations, and private entities, other collections from governmental entities, and authorizations by the Legislative of the Commonwealth of Puerto Rico, which are designed to attain specific purposes. The expenditures charged to these accounts are authorized by legislation previously approved.

### Basis of accounting

The **PRNG** follows a receipts and disbursements method of accounting to account for all funds administered under this method, cash or funds transfer-in are recognized as revenues when received, and expenditures are recognized when funds are disbursed or transferred-out. Therefore, the Statement of Receipts and Disbursements is not intended to present the **PRNG's** results of operations in accordance with generally accepted accounting principles in the United States of America.

### Budgetary accounting

Formal budgetary accounting is employed as a management control tool for all funds of the **PRNG**. Annual operating budgets are adopted each fiscal year through passage of an annual budget, which is approved by the Legislature of the Commonwealth of Puerto Rico and amended, if is required, throughout the year. Budgetary control procedures required the obligation of funds before purchase orders can be placed; it means that applicable appropriations must be reserved before purchase orders or contracts can be entered into. Obligated appropriations at year end carryover to the next fiscal year and are not reported as part of the next fiscal year's budget. For budgetary purposes, encumbrances accounting is used. The encumbrances (that is, purchase order and contracts) are considered expenditures when paid.



**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):**

**Excess (deficiency) statement line**

The excess (deficiency) of receipts over (under) disbursement statement line represents a summation of the combined receipts and disbursements. Consequently, amounts shown in this line is not comparable to an excess or deficiency over funds assigned and do not represent a deficit of the **PRNG**.

**Restriction of cash balances**

Restrictions of cash balance represent portions of cash balances that are legally segregated for a specific future use or are not appropriable for disbursements. The **PRNG** has the following restrictions of cash balances:

**Encumbrances** – Represent future expenditures under purchase orders, contracts, and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

**Federal cooperative agreements** – Represent monies to financial federal programs for operations and maintenance of military facilities and youth programs.

**Other purposes** – Represents future cash disbursements under purchase orders and commitments. These committed amounts represent a restriction of appropriations and generally will become cash disbursements in future periods as the goods or services are received.

**2. PENSION PLAN BENEFITS**

**General information about the pension plan**

As of June 30, 2016, regular employees of the **PRNG** contribute to a cost-sharing multiple employer hybrid defined benefit and defined contribution retirement plan administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). ERS covers all regular full-time public employees working for the central government, the municipalities of Puerto Rico and certain public corporations not having their own retirement systems. The system provides retirement pensions, death, and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation. The pension plan operates under Act No. 447 of May 15, 1951, as amended, Act No. 305 of September 24, 1999 (System 2000 Reform) and Act No. 3 of April 4, 2013.



## 2. PENSION PLAN BENEFITS (CONTINUED)

Under Act 447, retirement benefits were determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation was computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member was eligible, was limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. For active participants of the contributory defined benefit programs under Act No. 447, all retirement benefits accrued through June 30, 2013 were frozen. Thereafter, all future benefits will accrue under the hybrid pension plan established by Act No. 3. Participants will receive a pension at retirement age equivalent to what they had accrued under Act 447 up to June 30, 2013, and a supplemental annuity corresponding to contributions made after July 1, 2013.

Participants under the defined contribution plan established by Reform System 2000 will receive a lifetime annuity calculated at retirement based on a factor that will incorporate the individual's life expectancy and a rate of return. New participants under the hybrid plan established by Act No. 3 will receive a lifetime annuity based on the accumulated balance of their individual accounts (employees' contributions plus a return on investment). The minimum monthly pension for current retirees is \$500.

Disability benefits previously provided by Act No. 447 and Reform System 2000 were eliminated by Act No. 3 and substituted for a mandatory disability insurance policy. Beginning July 1, 2013, each employee must contribute to this insurance plan .25% of his or her monthly salary, up to a monthly maximum of \$5,000. Therefore, the maximum monthly employee contribution will be \$12.50 ( $\$5,000 \times .25\%$ ).

Beginning July 1, 2013, all employers must contribute 12.275% of employee contribution with an additional 1% annually up to June 30, 2016; after July 1, 2016, an additional 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective July 1, 2020. For the fiscal year ended June 30, 2016, the employer contribution rate was 14.275% and the total required annual contribution amounted to \$1,290,019.

As required by Act 32 of June 25, 2015, the Additional Uniform Contribution (AUC) was established for the purpose of solving the cash flow deficit of the System. For each fiscal year, beginning on July 1, 2013, the ERS will: 1) determine the portion of the AUC attributable to each participating employer based on the percentage each employer's contributions represent of the total employer contributions established for that fiscal year; and 2) send to the director of the P.R. Office of Management and Budget (OMB) and to each public corporation and municipality whose employees are covered by this Act, a certification of the AUC owed by each employer. The **PRNG's** AUC for the fiscal year 2015-16, amounted to \$145,402.

## 3. POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described in Note 2, the **PRNG** is required to cover annually the 3% increase in the retirement plan of its retired employees, as required by Commonwealth's laws. Also, the **PRNG** is required to finance costs related to the application of certain laws issued by the Commonwealth Government.



### 3. POSTEMPLOYMENT BENEFITS (CONTINUED)

Those laws granted increases in pensions and other benefits to retired employees of the **PRNG** such as medicines bonus, Christmas and summer bonuses and death benefits. However, beginning July 1, 2013, Act 3 of 2013 eliminated certain laws benefits to future retirees.

For the year ended June 30, 2016, the cost related to these post-employment benefits amounted to \$2,671,325, which were paid by the P.R. Office of Management and Budget (OMB) on behalf of the **PRNG**.

### 4. COMPENSATED ABSENCES

The vacation policy of the Commonwealth of Puerto Rico that applies to the employees of the **PRNG** provides for the accumulation of 2.5 days per month. Vacation time accumulated is fully vested to the employees from the first day of work up to a maximum of 60 days. Also, **PRNG's** employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated unpaid leave at a current rate, if the employee has at least ten (10) years of service with the Commonwealth of Puerto Rico.

### 5. TERMINATION BENEFITS

On July 2, 2010, the Commonwealth enacted Act No. 70 to establish a program that provides benefits for early retirement or economic incentives for voluntary employment termination to eligible employees, as defined, including employees of the **PRNG**. Act No. 70 establishes that early retirement benefits will be provided to eligible employees that have completed between 15 to 29 years of credited service in the Retirement System and will consist of biweekly benefits ranging from 37.5% to 50% of each employee's salary, as defined. In this early retirement benefit program, the **PRNG** will make the employee and the employer's contributions to the Retirement System and pay the corresponding pension until the employee complies with the requirement age and 30 years of credited service.

Economic incentives were available to eligible employees who had less than 15 years of credited service, who had at least 30 years of credited service and the age for retirement, or who had the age for retirement. Economic incentives consisted of a lump-sum payment ranging from one-month to six-month salary based on employment years. For eligible employees that chose the economic incentives and had at least 30 years of credited service and the age for retirement, or had the age for retirement, the **PRNG** will make the employee and the employer's contributions to the Retirement System for a five year period. Additionally, eligible employees that chose to participate in the early retirement benefit program, chose the economic incentive and had less than 15 years of credited service were eligible to receive health plan coverage for up to 12 months in a health plan selected by the management of the **PRNG**. During fiscal year ended June 30, 2016, payments for termination benefits made by the **PRNG** amounted to \$133,030.

**6. COMMITMENTS**

The **PRNG** rents its facilities through operating lease agreements with the Puerto Rico Industrial Development and the Puerto Rico Ports Authority, instrumentalities of the Commonwealth of Puerto Rico. The agreements with the governmental instrumentalities provide for rental fees significantly below market value. Rent disbursements under such lease agreements for the fiscal years ended June 30, 2016, were approximately **\$29,649**. As of the date of these financial statements were issued, the **PRNG** was negotiating various expired lease agreements, including some whose monthly payments have been withheld until the contract is renewed. Future minimum rental payments as of June 30, 2016 for the next five years and thereafter are as follows:

Year ending June 30,	<u>Amount</u>
2017	\$ 29,649
2018	32,428
2019	35,208
2020	35,208
2021	35,208
Thereafter	<u>176,040</u>
	<b>\$ 343,741</b> =====

**7. CONTINGENCIES**

**Litigation** - The **PRNG** is defendant in lawsuits arising in the normal course of operations, principally from claims for alleged violation of civil rights and discrimination in employment practices. According to the laws of the Commonwealth of Puerto Rico, the **PRNG** is fully represented by the Puerto Rico Department of Justice in defense of all legal cases against the **PRNG**. Any claims with negative financial impact will be paid from the General Fund of the Commonwealth of Puerto Rico, with no effect on the budget or resources of the **PRNG**.

**Federal Awards** - The **PRNG** participates in a number of federal financial assistance programs funded by the Federal Government. Expenditures financed by these programs are subject to financial and compliance audits by the appropriated grantors or their representatives. If expenditures are disallowed due to noncompliance with grant program regulations, the **PRNG** may be required to reimburse the grantors for such expenditures.



## 7. CONTINGENCIES (CONTINUED)

### **Puerto Rico Fiscal and Economic Growth Plan**

On September 9, 2015, the Working Group for the Fiscal and Economic Recovery of Puerto Rico established by the Governor Alejandro García Padilla by executive order EO 2015-022 submitted the Fiscal and Economic Growth Plan (FEGP), setting forth economic development, structural, fiscal and institutional reform measures intended to meaningfully reduce the Commonwealth's projected financing gaps. In order to ensure compliance with the FEGP measures, the Working Group proposes the implementation of a Control Board and new budgetary regulations, pursuant to proposed legislations known as the Fiscal Responsibility and Economic Revitalization Act (FRERA). The reform measures proposed by the FEGP, including the creation of the Control Board, have been submitted to the Commonwealth Legislature for review and final approval.

All the economic plans prepared and developed by the Government of Puerto Rico, shall be reviewed and approved by the Board established the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA)

### **Puerto Rico Emergency Moratorium and Financial Rehabilitation Act**

The Legislature Assembly of the Commonwealth of Puerto Rico resolved to provide the Governor with powers to declare a state of emergency for the Commonwealth and its instrumentalities, including the Governmental Development Bank (GDB), and declare a moratorium on the payment of certain obligations of those entities. Accordingly, on April 6, 2016, the Legislature approved Act No. 21, known as the Puerto Rico Emergency Moratorium and Financial Rehabilitation Act (the Act). This Act empowers the Governor with narrowly tailored authority within the boundaries of the Commonwealth's laws and Constitution, to enable the Commonwealth and its instrumentalities to continue providing essential services to Puerto Rico's residents while addressing the critical need for structural and fiscal reform and debt.

The Act provides for moratorium measures that are temporary in nature and only apply upon a finding by the Governor that invoking the provisions of the Act is necessary to provide for health, safety, and welfare of the residents of the Commonwealth. Further, such measures (including the stay on creditor actions) are invoked on an entity-by-entity basis and, without a specification by the Governor of further enumerated obligations, only affect limited financial indebtedness obligations coming due during a temporary period.

In addition, the measures set forth in the Act are crafted with due regard to the rights of Puerto Rico's creditors. The Act does not provide for a composition or discharge of debts; instead, all claims and priorities are preserved, and any unpaid amounts on the obligations of the Commonwealth and its instrumentalities are not forgiven and instead are payable, as set forth in the Act, at the end of any moratorium period to the extent permitted by otherwise applicable law. Further, the Act respects Constitutional priorities by establishing minimum criteria for the payment of the Commonwealth's public debt that may come due during the temporary moratorium period.



## 7. CONTINGENCIES (CONTINUED)

### **Puerto Rico Emergency Moratorium and Financial Rehabilitation Act**

On April 8, 2016, the Governor signed the Executive Order No. 2016-010 ("EO No. 2016-010) declaring the GDB to be in a state of emergency pursuant to Act No. 21 and imposing on the GDB certain operational restrictions and debt moratorium.

Also, on April 30, the Governor signed the Executive Order No. 2016-014 ("EO No. 2016-014) and pursuant the provisions established on this order, on May 1, 2016, the GDB failed to make a principal payment of approximately \$367 million in respect of its notes.

Furthermore, on July 1, 2016, the Commonwealth failed to make a principal payment of approximately \$1.1 billion in respect of its General Obligation Bonds.

### **Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA)**

On June 30, 2016, the U.S. President signed the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA), which grants the Commonwealth and its component units access to an orderly mechanism to restructure their debts in exchange for significant federal oversight over the Commonwealth's finances. In general, PROMESA seeks to provide Puerto Rico with fiscal and economic discipline through the creation of a Control Board, relief from creditor lawsuits through the enactment of a temporary stay on litigation, and two alternative methods to adjust unsustainable debt. To ensure fiscal and economic discipline, PROMESA creates a federally appointed oversight board (the Board) that has plenary authority over Puerto Rico's finances.

The board's primary function is to provide fiscal oversight through the development and approval of fiscal plans and budgets, and to enforce compliance with those plans and budgets. The Board also has oversight over legislative processes because PROMESA requires the Board to review new laws and deny their enforcement if they are inconsistent with the approved fiscal plans and budgets. The Board also has authority to review contracts to ensure compliance with the fiscal plan, and to prevent the execution or enforcement of a contract, rule, executive order or regulation to the extent that it is inconsistent with the approved fiscal plan.

The enactment of PROMESA also operates as a broad-based stay on litigation, applicable to all entities, with respect to claims related Puerto Rico's financial debt, as well as on enforcement of provisions in contracts that allow for termination and the exercise of remedies based on non-payment of financial obligations, among other conditions.

In addition, PROMESA contains two (2) mechanisms to adjust Puerto Rico's debts. The first mechanism is a streamlined process to achieve modifications of financial indebtedness with the consent of a supermajority of affected financial creditors. The second mechanism is a court-supervised debt-adjustment process, which is modeled on Chapter 9 of the U.S. Bankruptcy Code.

## 7. CONTINGENCIES (CONTINUED)

### Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) (Continued)

The Commonwealth expects that its ability to finance future budget deficits will be severely limited even if it achieves a comprehensive debt restructuring, and, therefore, that it will be required to, among other measures, reduce the amount of resources that fund important governmental programs and services in order to balance its budget. There is no assurance, however, that budgetary balance will be achieved and, if achieved, that such budgetary balance will be based on recurring revenue or expense reductions or that the revenue or expense measures undertaken to balance the budget will be sustainable on a long term basis. Accordingly, there is no assurance that the federally appointed oversight board of PROMESA will be successful in achieving budgetary and fiscal balance through a debt restructuring or otherwise.

## 8. SUBSEQUENT EVENTS

Subsequent events were evaluated through March 22, 2017, the date the financial statements were available to be issued. No significant events that should have been recorded or disclosed in the financial statements were noted, except for the event described in the following paragraph.

The Commonwealth and its public entities have not been able to repay been able to repay its loans from the GDB. This situation has significantly affected the GDB's liquidity and ability to repay its obligations. Accordingly, the GDB faces significant risks and uncertainties and it currently does not have sufficient liquid financial resources to meet obligations when they are due. Therefore, on May 1, 2016, the GDB failed to make a principal payment of approximately \$367 million in respect of its notes.

On October 18, 2016, the Department of Treasury of Puerto Rico issued Circular Letter No. 1300-08-17, which applied to all Public Corporations and Instrumentalities of the Commonwealth, and all Municipalities. This Circular Letter states that an assessment of a possible loss shall be made on cash and investments deposited on the GDB. Any impairment loss resulting from this evaluation shall be recognized during the fiscal year ended June 30, 2016.

As described on Note 1, the **PRNG's** financial statements are prepared using the cash receipts and cash disbursements method of accounting. Therefore, the Statement of Receipts and Disbursements is not intended to present the **PRNG's** results of operations in accordance with generally accepted accounting principles in the United States of America. Accordingly, no impairment adjustment is presented in such statements.



	Budgeted Amounts		Actual Budgetary Basis (See Note 1)	Variance Positive (Negative)
	Original Budget	Final Amended Budget		
<b>Resources (inflows):</b>				
Amounts available for appropriations	\$ 11,743,000	\$ 9,659,000	\$ 9,659,000	\$ -
<b>Charges to appropriations (outflows):</b>				
Payroll and related expenses	4,712,000	6,003,647	6,003,647	-
Facilities and payments for services	1,838,000	70,000	70,000	-
Purchased services	564,000	50,032	50,032	-
Material and supplies	12,000	52,633	52,633	-
Federal matching fund allocation	3,745,000	3,413,584	3,413,584	-
Transportation expenses	12,000	7,000	7,000	-
Other operating expenses	860,000	62,104	62,104	-
Total charges to appropriations	11,743,000	9,659,000	9,659,000	-
<b>Budgetary fund balance, June 30, 2016</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

See notes to Budgetary Comparison Schedule.

**1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**Budgetary Control**

A budget is prepared for the General Fund and represents legislative appropriations for the general operation of the **PRNG**. The procedures followed for the approval and operations of the budget are defined by the laws of the Commonwealth of Puerto Rico. The **PRNG** submits to the Office of Management and Budget of the Commonwealth of Puerto Rico its budget request. Then, the Governor submits the budget of the central government of the Commonwealth to the Legislative Council in the House of Representatives and Senate. The budget is legally adopted through an Act of the Legislative Council approved by the Governor. Formal budgetary information is employed as a management control device during the year for the general fund. Actual expenditures may not legally exceed budget appropriations for each of the classifications, which are shown in the budgetary statement. In instance were budget revenues and appropriations have been revised during the year, budgets amounts presented in the financial statements represent final authorization amounts. Available appropriations and encumbrances lapse one year after end of the fiscal year. The budget is adopted in accordance with a budgetary basis of accounting which differs from USGAAP. The Commonwealth of Puerto Rico Department of Treasury and the Office of Management and Budget have the responsibility to ensure that budgetary spending control is maintained on an individual appropriation account basis. Budgetary control is exercised through the PRIFAS Accounting System. The **PRNG** should maintain its own accounting records, which should be periodically reconciled with PRIFAS' Integrated Financial Accounting System.

The reconciliation in the general fund of the differences between statutory budgetary/cash receipt and disbursement basis for the fiscal year ended June 30, 2016 is as follows:

Excess of cash appropriation determined in accordance with the statutory basis of accounting as presented in the Budgetary Comparison Schedule – General Fund –budgetary basis	\$ -
Add: Current year encumbrances recognized as expenditures for budget purposes	2,912,115
Less: Expenditures paid with prior year encumbrances recognized as disbursements under the cash basis of accounting	<u>(1,552,453)</u>
Excess of cash disbursements, determined in accordance with the cash receipts and disbursement basis of accounting	<u>\$ 1,359,662</u>



<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Federal Expenditures</u>	<u>Passed to Subrecipient</u>
<b>CASH ASSISTANCE:</b>				
<b><u>U.S Department of Defense National Guard Bureau</u></b>				
<b>Direct Program:</b>				
National Guard Military Operations and Maintenance (O&M) Projects	12.401	N/A	\$ 18,953,340	\$ -
National Guard Challenge Program	12.404	N/A	3,816,185	-
			<u>\$ 22,769,525</u>	<u>\$ -</u>

The accompanying notes are an integral part of this schedule.

## 1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal grant activity of the **National Guard of the Commonwealth of Puerto Rico (the PRNG)** under programs of the federal government for the year ended June 30, 2016. The information in this Schedule is presented in accordance with the requirements of OMB Uniform Guidance, Audits of States, Local Governments, and Non-Profits Organizations. Because the Schedule presents only a selected portion of the operations of the **PRNG**, it is not intended to and does not purport to present the financial position, changes in net position, or cash flows of the **PRNG**.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICES

- a. Expenditures reported on the Schedule are reported on the receipts and disbursements method of accounting. It is drawn primarily from the **PRNG's** internal accounting records, which are the basis for the **PRNG's** Statement of Receipts and Disbursements. Such expenditures are recognized following the cost principles contained in the OMB Uniform Guidance, *Cost Principles for States, Local, and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.
- b. The titles of federal awards included in the Schedule are presented as described in the Catalog of Federal Domestic Assistance.

State or local government redistributions of federal awards to the **PRNG**, known as "pass-through awards" should be treated by the **PRNG** as though they were received directly from the federal government. The Uniform Guidance requires the Schedule to include the name of the "pass-through entity" and the identifying number assigned by the "pass-through entity" for the federal awards received as a sub-recipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

## 3. RELATIONSHIP TO THE STATEMENT

Expenditures included in the Schedule agree with the amounts included in the accompanying Statement of Receipts and Disbursements – Governmental Funds.

## 4. INDIRECT COST RATE

The **PRNG** has elected not to use the ten percent of the minimum indirect cost rate allowed under the Uniform Guidance.





López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

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

**National Guard of the  
Commonwealth of Puerto Rico  
San Juan, Puerto Rico**

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States of America, the financial statements – cash basis of the governmental activities, each major fund, and the aggregated remaining fund information arising from cash transactions of the **National Guard of the Commonwealth of Puerto Rico (the PRNG)**, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the **PRNG's** basic financial statements as listed in the table of contents, and have issued our report thereon dated March 22, 2017.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered **PRNG'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 **PRNG's** internal control. Accordingly, we do not express an opinion on the effectiveness of the **PRNG's** internal control.

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

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

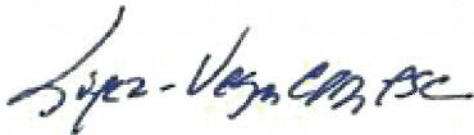
**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS (CONTINUED)**

**Compliance and Other Matters**

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

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the **PRNG'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 **PRNG's** internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



**LOPEZ-VEGA, CPA, PSC**

San Juan, Puerto Rico  
March 22, 2017  
Stamp No. 2728540 of the Puerto Rico  
Society of Certified Public Accountants  
was affixed to the record copy of this report.





*López-Vega, CPA, PSC*

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON  
INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE**

**National Guard of the  
Commonwealth of Puerto Rico  
San Juan, Puerto Rico**

**Report on Compliance for Each Major Federal Program**

We have audited the **National Guard of the Commonwealth of Puerto Rico's (the PRNG)** compliance with the types of compliance requirements described in the OMB Compliance Supplement that could have direct and material effect on each of the **PRNG's** major federal programs for the year ended June 30, 2016. The **PRNG's** major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

**Management's Responsibility**

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

**Auditors' Responsibility**

Our responsibility is to express an opinion on compliance for each of the **PRNG's** major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Costs Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **PRNG's** compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the **PRNG's** compliance.

**Opinion on Federal Grant Programs**

In our opinion, the **PRNG** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON  
INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE (CONTINUED)**

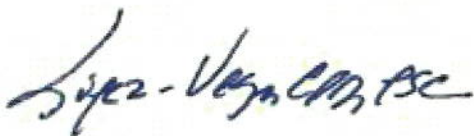
**Report on Internal Control over Compliance**

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

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

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

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



**LOPEZ-VEGA, CPA, PSC**

San Juan, Puerto Rico

March 22, 2017

Stamp No. 2728541 of the Puerto Rico

Society of Certified Public Accountants

was affixed to the record copy of this report.



*López-Vega, CPA, PSC*

Certified Public Accountants / Management Advisors



**Section I - Summary of Auditors' Report**

1. The auditors' report expresses an unmodified opinion on the financial statements of the **PRNG**.
2. No significant control deficiencies were disclosed during the audit of the financial statements.
3. No instance of noncompliance material to the financial statements of the **PRNG** was disclosed during the audit.
4. No significant deficiency or instance of non-compliance on internal control over compliance with requirements applicable to major federal programs was disclosed during the audit.
5. The auditors' report on compliance for each of the major federal award programs for the **PRNG** expresses an unmodified opinion on its major federal programs.
6. There are not audit findings that require to be reported in accordance with the OMB Uniform Guidance.
7. The programs tested as major include:

**CFDA Number**

**Name of Federal Program or Cluster**

12.401

National Guard Military Operations  
and Maintenance (O & M) Project

8. The threshold for distinguishing Types A and B programs was **\$750,000**.
9. The **PRNG** was not determined to be a low-risk auditee.

**Section II – Financial Statements Findings**

During our audit, we did not detect deficiencies, significant deficiencies, material weaknesses, or instances of noncompliance related to the basic financial statements that are required to be reported in accordance with Government Auditing Standards.



**Section III - Major Federal Award Program Findings and Questioned Costs**

During our audit, we did not detect deficiencies, significant deficiencies, material weaknesses, or instances of noncompliance related to the basic financial statements that are required to be reported in accordance with the OMB Uniform Guidance.

