Puerto Rico Medical Services Administration
A Component Unit of the
Puerto Rico Department of Health

Financial Statements

June 30, 2016 and 2015

(Restated)

Table of Contents

Management's Discussion and Analysis	1-14
Independent Auditors' Report	15-18
Financial Statements:	
Statements of Net Position	19
Statements of Revenues, Expenses and Changes in Net Position (Deficit)	20
Statements of Cash Flows	21-22
Notes to Financial Statements	23-73

Management's Discussion and Analysis

The following discussion and analysis of the Puerto Rico Medical Services Administration (the Administration) provides an overview of the Administration's financial performance during the years ended June 30, 2016 and 2015. Please read it in conjunction with the basic financial statements, which follow this section.

Financial Highlights

1. The Administration's net position (deficit) as of June 30, 2016 and 2015 amounted to approximately ($873) million and ($739) million, respectively.

2. During the years ended June 30, 2016 and 2015 the Administration experienced operating losses of approximately $139 and $69 million, respectively.

3. During the years ended June 30, 2016 and 2015, the Administration received approximately $28 and $47 million, respectively, in contributions from governmental agencies, for payment of new recruitments, payroll contributions and other operating expenses.

Required Financial Statements

The required basic financial statements of the Administration consist of:

1. Statement of net position – The statement of net position includes all of the Administration's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for evaluating the net assets' structure of the Administration and assessing its liquidity and financial flexibility.

2. Statement of revenues, expenses and changes in net position – This statement measures the results of the Administration's operations and can be used to determine whether the Administration has successfully recovered operating costs and expenses through services revenues, contributions, and other non-operating income.

3. Statement of cash flows – This statement reports cash receipts, cash payments, and net changes resulting from operating, investing, and capital and non-capital related financing activities.

Statements of Net Position

The Administration's statements of net position as of June 30, 2016 and 2015 consisted of (in thousands):

	2016 (As restated)	2015 (As restated)	Increase (Decrease)	%
Current assets	$ 55,033	$ 46,393	$ 8,640	19%
Non-current assets:				
Capital assets, net	56,282	59,413	(3,131)	-5%
Restricted cash	3,338	1,166	2,172	186%
Other non-current assets	1,850	15,845	(13,995)	-88%
	61,470	76,424	(14,954)	-20%
Total assets	116,503	122,817	(6,314)	-5%
Deferred outflows of resources	121,732	85,862	35,870	42%
Current liabilities	199,386	147,873	51,513	35%
Non-current liabilities	901,526	796,997	104,529	13%
Total liabilities	1,100,912	944,870	156,042	17%
Deferred inflows of resources	10,565	3,186	7,379	232%
Net position:				
Net investment in capital assets	56,282	59,413	(3,131)	-5%
Restricted	629	535	94	100%
Unrestricted (deficit)	(930,153)	(799,325)	(130,828)	16%
Total net position (deficit)	$ (873,242)	$ (739,377)	$ (133,865)	18%

The Administration's statements of net position as of June 30, 2015 and 2014 consisted of (in thousands):

	2015 (As restated)	2014 (As restated)	Increase (Decrease)	%
Current assets	$ 46,393	$ 40,504	$ 5,889	15%
Non-current assets:				
Capital assets, net	59,413	59,865	(452)	-1%
Restricted cash	1,166	957	209	22%
Other non-current assets	15,845	20,171	(4,326)	-21%
	76,424	80,993	(4,569)	-6%
Total assets	122,817	121,497	1,320	1%
Deferred outflows of resources	85,862	-	85,862	100%
Current liabilities	147,873	125,298	22,575	18%
Non-current liabilities	796,997	693,823	103,174	15%
Total liabilities	944,870	819,121	125,749	15%
Deferred inflows of resources	3,186	-	3,186	100%
Net position:				
Net investment in capital assets	59,413	59,865	(452)	-1%
Restricted	535	271	264	100%
Unrestricted (deficit)	(799,325)	(757,760)	(41,565)	5%
Total net position (deficit)	$ (739,377)	$ (697,624)	$ (41,753)	6%

Statements of Net Position

The increase in current assets as of June 30, 2016, consisted of (in thousands):

	2016	2015	Increase (Decrease)	%
Unrestricted cash	$ 560	$ 1,754	$ (1,194)	-68%
Receivable from member institutions and private insurances	49,487	39,745	9,742	25%
Note receivable	850	800	50	6%
Accounts receivable others	58	48	10	21%
Inventories	3,568	3,557	11	0%
Prepaid expenses	510	489	21	4%
	$ 55,033	$ 46,393	$ 8,640	19%

The increase in current assets as of June 30, 2015, consisted of (in thousands):

	2015	2014	Increase (Decrease)	%
Unrestricted cash	$ 1,754	$ 1,098	$ 656	60%
Receivable from member institutions and private insurances	39,745	35,018	4,727	13%
Note receivable	800	-	800	100%
Accounts receivable others	48	67	(19)	-28%
Inventories	3,557	3,469	88	3%
Prepaid expenses	489	852	(363)	-43%
	$ 46,393	$ 40,504	$ 5,889	15%

This Space Is Intentionally Left In Blank

Statements of Net Position – (continued)

The net increase (decrease) in accounts receivable from member institutions and private insurances, consisted of the following activity during the years ended June 30, 2016 and 2015 (in thousands):

As of June 30, 2016:

	Member Institutions	Private Insurance	Total
Gross services revenues	$ 101,309	$ 124,787	$ 226,096
Revenue accounts reclassification	1,672	(1,723)	(51)
Contractual adjustments	-	(78,386)	(78,386)
Collections from prior years	-	587	587
Non cash transactions	(263)	-	(263)
Provision for bad debt expense	(3,531)	(13,279)	(16,810)
Collections	(87,172)	(34,259)	(121,431)
	$ 12,015	$ (2,273)	$ 9,742

As of June 30, 2015:

	Member Institutions	Private Insurance	Total
Gross services revenues	$ 101,002	$ 120,926	$ 221,928
Revenue accounts reclassification	1,048	(1,012)	36
Contractual adjustments	-	(68,710)	(68,710)
Collections from prior years	-	1,099	1,099
Non cash transactions	(3,811)	-	(3,811)
Provision for bad debt expense	(4,923)	(13,163)	(18,086)
Collections	(86,333)	(41,396)	(127,729)
	$ 6,983	$ (2,256)	$ 4,727

The increase of $9,742 million in accounts receivable is mainly due to the 5% increase in service charges to Members Institutions and a reduction of bad debt expense. During 2016 there was a 5% or $9,676 million increase in contractual adjustment expense due to the 5% increase in sales prices approved by the Board of Participating Entities and 5% or $6,298 million reduction in collections.

Statements of Net Position – (continued)

Non-Current Assets - Capital Assets

As of June 30, 2016:

Description	Balance June 30, 2015	Increase	Decrease	Balance June 30, 2016
Capital assets not being depreciated	$ 6,872	$ -	$ -	$ 6,872
Capital assets being depreciated	181,952	1,832	(187)	183,597
Accumulated depreciation	(129,411)	(5,054)	278	(134,187)
Capital assets being depreciated, net	52,541	(3,222)	91	49,410
Capital assets, net	$ 59,413	$ (3,222)	$ 91	$ 56,282

As of June 30, 2015:

Description	Balance June 30, 2014	Increase	Decrease	Balance June 30, 2015
Capital assets not being depreciated	$ 6,872	$ -	$ -	$ 6,872
Capital assets being depreciated	178,038	4,547	(633)	181,952
Accumulated depreciation	(125,045)	(4,974)	608	(129,411)
Capital assets being depreciated, net	52,993	(427)	(25)	52,541
Capital assets, net	$ 59,865	$ (427)	$ (25)	$ 59,413

The decrease in capital assets during the year ended June 30, 2016 is mainly due to the fact that current year depreciation expense exceeded acquisitions of equipment and building improvements.

This Space Is Intentionally Left In Blank

Statements of Net Position – (continued)

Liabilities

Current liabilities

The increase in current liabilities consisted of (in thousands):

	2016	2015	Increase (Decrease)	%
Accounts payable	$ 82,849	$ 71,940	$ 10,909	15%
Accrued expenses	5,574	6,669	(1,095)	-16%
Accrued interest	30,091	13,145	16,946	129%
Current portion accrued pension costs	71,160	48,030	23,130	48%
Current portion of compensated absences	9,256	7,428	1,828	25%
Liabilities payable from restricted assets	456	661	(205)	-31%
	$ 199,386	$ 147,873	$ 51,513	35%

	2015	2014	Increase (Decrease)	%
Accounts payable	$ 71,940	$ 68,899	$ 3,041	4%
Accrued expenses	6,669	9,424	(2,755)	-29%
Accrued interest	13,145	16,671	(3,526)	-
Current portion accrued pension costs	48,030	25,859	22,171	86%
Current portion of compensated absences	7,428	314	7,114	2266%
Liabilities payable from restricted assets	661	4,131	(3,470)	-84%
	$ 147,873	$ 125,298	$ 22,575	18%

The increase of $10,909 in accounts payable and $23,130 in accrued pension cost was mainly due to the deficiency of cash flow to pay debts in the Administration during the year ended June 30, 2016. The increase of $16,946 million in accrued interest is because the Commonwealth of Puerto Rico didn't make the payment corresponding to the GDB line of credit of this year, as per Law 66 of June 22, 1978.

Statements of Net Position – (continued)

Non-current liabilities

The decrease in non-current liabilities as of June 30, 2016, consisted of (in thousands):

	2016 (As restated)	2015 (As restated)	Increase (Decrease)	%
Government Development Bank of Puerto Rico line of credit in connection with Law #66 of June 22, 1978, as amended	$ 282,448	$ 282,445	$ 3	0%
Net pension liability	609,077	504,172	104,905	21%
Accrued pension costs, net of current portion	-	1,023	(1,023)	-100%
Compensated absences, net of current portion	5,867	5,079	788	16%
Other post-employment benefit obligations	1,834	1,834	-	0%
Liabilities payable from restricted assets-Self insurance fund	2,300	2,444	(144)	-6%
	$ 901,526	$ 796,997	$ 104,529	12%

During fiscal year 2015, the Administration restated the financial statements to adopt the Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions,* an amendment of GASB Statement No. 27, and GASB Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date,* an amendment of GASB Statement No. 68. The impact of adopting the statements consisted of recognizing the net effects of the Administration's proportionate share of Employee's Retirement System's beginning net pension liability and deferred outflows of resources for pension contributions made after the beginning net pension liability measurement date.

The decrease in other non-current liabilities is mainly due to the decrease in accrued pension cost of $1,023 due to payments made under the agreement with the Commonwealth of Puerto Rico and increase of $788 in compensated absences, net by the decrease in liabilities payable from restricted assets in Self insurance fund.

This Space Is Intentionally Left In Blank

Statements of Net Position – (continued)

Non-Current Liabilities

The following is the activity of non-current liabilities for the years ended June 30, 2016 and 2015 (in thousands):

As of June 30, 2016: Description	Balance June 30, 2015 (As restated)	Increase	Decrease	Balance June 30, 2016 (As restated)
Self-insurance fund	$ 2,444	$ 18	$ (162)	$ 2,300
Accrued pension costs, net of current portion	1,023	-	(1,023)	-
Compensated absences, net of current portion	5,079	788	-	5,867
Other post-employment benefit obligation	1,834	-	-	1,834
Government Development Bank of Puerto Rico line of credit in connection with Law #66 of June 22, 1978 as amended	282,445	3	-	282,448
Net pension liability	504,172	104,905	-	609,077
	$ 796,997	$ 105,714	$ (1,185)	$ 901,526

As of June 30, 2015: Description	Balance June 30, 2014 (As restated)	Increase	Decrease	Balance June 30, 2015 (As restated)
Self-insurance fund	$ 2,800	$ 5	$ (361)	$ 2,444
Accrued pension costs, net of current portion	4,091	-	(3,068)	1,023
Compensated absences, net of current portion	11,508	-	(6,429)	5,079
Other post-employment benefit obligation	1,834	-		1,834
Government Development Bank of Puerto Rico line of credit in connection with Law #66 of June 22, 1978 as amended	278,292	4,153	-	282,445
Net pension liability	395,298	108,874	-	504,172
	$ 693,823	$ 113,032	$ (9,858)	$ 796,997

Revenues, Expenses and Changes in Net Position

The Administration's statements of revenue, expenses, and changes in net position for the years ended June 30, 2016 and 2015, consisted of (in thousands):

	2016 (As restated)	2015 (As restated)	Increase (Decrease)	%
Net service revenues	$ 131,486	$ 136,230	$ (4,744)	-3%
Operating costs and expenses:				
Cost of services	161,436	158,721	2,715	2%
General and administrative	14,668	15,316	(648)	-4%
Depreciation and amortization	5,054	4,974	80	2%
Provision for bad debts	13,144	-	13,144	100%
Pension expense	76,414	26,198	50,216	192%
	270,716	205,209	65,507	32%
Operating loss	(139,230)	(68,979)	(70,251)	102%
Non-operating income (expenses):				
Contributions from the Commonwealth of Puerto Rico	27,769	46,609	(18,840)	-40%
Other income	(23)	638	(661)	-104%
Interest expenses	(22,378)	(19,996)	(2,382)	12%
Loss on disposition of capital assets	(3)	(25)	22	-88%
	5,365	27,226	(21,861)	-80%
Net change in net position	(133,865)	(41,753)	(92,112)	221%
Net position (deficit), at beginning of year	(739,377)	(697,624)	(41,753)	6%
Net position (deficit), at end of year	$ (873,242)	$ (739,377)	$ (133,865)	18%

The Administration's statements of revenue, expenses, and changes in net position for the years ended June 30, 2015 and 2014, consisted of (in thousands):

	2015 (As restated)	2014 (As restated)	Increase (Decrease)	%
Net service revenues	$ 136,230	$ 123,143	$ 13,087	11%
Operating costs and expenses:				
Cost of services	158,721	166,613	(7,892)	-5%
General and administrative	15,316	17,068	(1,752)	-10%
Depreciation and amortization	4,974	4,589	385	8%
Pension expense	26,198	-	26,198	100%
	205,209	188,270	16,939	9%
Operating loss	(68,979)	(65,127)	(3,852)	6%
Non-operating income (expenses):				
Contributions from the Commonwealth of Puerto Rico	46,609	50,533	(3,924)	-8%
Other income	638	745	(107)	-14%
Decrease in self-insurance reserve	-	145	(145)	-
Interest expenses	(19,996)	(17,234)	(2,762)	16%
Loss on disposition of capital assets	(25)	(73)	48	-66%
	27,226	34,116	(6,890)	-20%
Transfer to the Commonwealth of Puerto Rico	-	(2,250)	2,250	100%
Net change in net position	(41,753)	(33,261)	(8,492)	26%
Net position (deficit), at beginning of year, as previously reported	(697,624)	(269,065)	(428,559)	159%
Prior period adjustment	-	(395,298)	395,298	100%
Net position (deficit), at end of year, as restated	$ (739,377)	$ (697,624)	$ (41,753)	6%

Revenues, Expenses and Changes in Net Position – (continued)

Net patient service revenues

The decrease in net service revenues for the year ended June 30, 2016, consisted of (in thousands):

	2016	2015	Increase (Decrease)	%
Member institutions	$ 101,309	$ 101,002	$ 307	0%
Private and insurance	46,400	52,215	(5,815)	-11%
Subtotal	147,709	153,217	(5,508)	
Provision for bad debts	(16,810)	(18,086)	1,276	-7%
Collection from prior years	587	1,099	(512)	0%
Subtotal	(16,223)	(16,987)	764	
	$ 131,486	$ 136,230	$ (4,744)	-3%

Approximately 74% of the Administration's net patient service revenues are derived from services rendered to member institutions. The decrease of $5,508 million in patient service revenue was due to the reduction in patients attended despite the efforts of the Administration improvement in the billing process, renegotiated some commercial health insurance contracts, institutional arrangements and increasing the sales prices to recover their cost. The decrease of $1,276 million in the provision of bad debt expense is principally caused by the reduction in reserve of Member Institutions.

The increase in net service revenues for the year ended June 30, 2015, consisted of (in thousands):

	2015	2014	Increase (Decrease)	%
Member institutions	$ 101,002	$ 90,790	$ 10,212	11%
Private and insurance	52,215	44,476	7,739	17%
Subtotal	153,217	135,266	17,951	
Provision for bad debts	(18,086)	(14,219)	(3,867)	27%
Collection from prior years	1,099	2,096	(997)	0%
Subtotal	(16,987)	(12,123)	(4,864)	
	$ 136,230	$ 123,143	$ 13,087	11%

Revenues, Expenses and Changes in Net Position – (continued)

Net patient service revenues – (continued)

Approximately 69% of the Administration's net patient service revenues are derived from services rendered to member institutions. The increase of $17,951 in patient service revenue was due to the Administration improvement in the billing process and it renegotiated some commercial health insurance contracts and institutional arrangements. The increase of $3,867 in the provision of bad debt expense is principally caused by the institutional arrangement of Outpatient Clinics with the School of Medicine.

Operating Costs and Expenses

Increase in operating costs and expenses for the year ended June 30, 2016, consisted of (in thousands):

	2016 (As restated)	2015 (As restated)	Increase (Decrease)	%
Salaries payroll taxes and fringe benefits	$ 100,256	$ 99,834	$ 422	0%
General and administrative	14,668	15,316	(648)	-4%
Costs of materials and services	55,498	51,452	4,046	8%
Depreciation and amortization	5,054	4,974	80	2%
Utilities	5,682	7,435	(1,753)	-24%
Provision for bad debts	13,144	-	13,144	100%
Pension expense	76,414	26,198	50,216	192%
	$ 270,716	$ 205,209	$ 65,507	32%

Increase in operating costs and expenses for the year ended June 30, 2015, consisted of (in thousands):

	2015 (As restated)	2014	Increase (Decrease)	%
Salaries payroll taxes and fringe benefits	$ 99,834	$ 104,736	$ (4,902)	-5%
General and administrative	15,316	17,068	(1,752)	-10%
Costs of materials and services	51,452	52,863	(1,411)	-3%
Depreciation and amortization	4,974	4,589	385	8%
Utilities	7,435	9,014	(1,579)	-18%
Pension expense	26,198	-	26,198	100%
	$ 205,209	$ 188,270	$ 16,939	9%

Revenues, Expenses and Changes in Net Assets (Deficit) – (continued)

Non-Operating Income (Expenses)

The decrease in non-operating income (expenses) for the year ended June 30, 2016 consists of (in thousands):

	2016	2015	(Decrease)	%
Governmental contributions	$ 27,769	$ 46,609	$ (18,840)	-40%
Other income	(23)	638	(661)	-104%
Interest expense	(22,378)	(19,996)	(2,382)	12%
Loss on disposition of capital assets	(3)	(25)	22	-88%
	$ 5,365	$ 27,226	$ (21,861)	-80%

The governmental contributions consisted of the following activity during the year ended June 30, 2016:

- $26.9 million received in connection with Joint Resolution No. 63 approved by the Commonwealth's Legislature Assembly on July 1, 2015, assigning to the Administration $26.9 million for the payment of salaries and operating expenses.
- $480,000 received in connection with Joint Resolution of Special Assignment No. 17-2013.
- $402,000 received in connection with a fund request for the acquisition of medical equipment.

Non-Operating Income (Expenses)

Interest expense during the years ended on June 30, 2016 and 2015 consisted principally of approximately $16.9 million each year billed mainly by the Government Development Bank of Puerto Rico and $5.3 million in 2016 for not complying with the payments of the obligations of the Employees' Retirement System.

Contacting the Administration's Financial Management

The financial report is designed to provide our suppliers and creditors with a general overview of the Administration's finances and to show the Administration's accountability for the funds it receives. If you have questions about this report or need additional financial information, contact the Administration's Finance Director Office at P.O. Box 2129 San Juan Puerto Rico 00936, phone no. (787) 777-3535 Ext. 2903.

INDEPENDENT AUDITORS' REPORT

The Secretary of the Puerto Rico Department of Health
and Board of Member Institutions of
Puerto Rico Medical Services Administration

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Puerto Rico Medical Services Administration (the Administration), a component unit of the Puerto Rico Department of Health (the Department), as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Administration's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Russell Bedford taking you further
Member of Russell Bedford International - a global network of independent professional services firms
www.fpvgalindez.com | PO Box 364152, San Juan, PR 00936-4152
Phone 787.725.4545 | 787.764.5049 Fax 787.724.5802 | 787.764.0528
TRUST worthy

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the Puerto Rico Medical Services Administration, as of June 30, 2016 and 2015, and the related changes in net position, and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 12 to the financial statements, the Administration derives a substantial portion of its revenues from services rendered to member institutions. In addition, the Administration provides services to the medical indigent population, some of them uninsured, which do not have formal means of repayment. Amounts due from member institutions and medical indigent population may be subject to periodic revisions and/or adjustments, based on the availability of funds from the member institutions and/or the entities adhered to the Commonwealth of Puerto Rico.

On June 30, 2016, the Puerto Rico Oversight, Management, and Economic Stability Act, Pub. Law 114-187 ("PROMESA" OR THE "Act"), was enacted into law. This Act establishes an Oversight Board to assist the Government of Puerto Rico, including instrumentalities, in managing its public finances, and for other purposes. On September 30, 2016, the Administration was identified as one of the covered entities subject to oversight under this Act.

On May 3, 2017, the Financial Oversight and Management Board for Puerto Rico (the "Oversight Board"), on behalf of the Commonwealth of Puerto Rico ("Puerto Rico"), filed a petition for relief under Title III of the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") in the United States District Court for the District of Puerto Rico.

The accompanying financial statements have been prepared assuming that the Administration will continue as a going concern. As discussed in Note 14 to the financial statements, the Administration has suffered recurring losses and has a negative financial position. These conditions raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 14. The financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Administration be unable to continue as a going concern.

Our opinion is not modified with respect to these matters.

As discussed in Note 1 to the financial statements, the accompanying financial statements present only the financial position and transactions attributable to the Administration. They do not intent to present, and do not present, the financial position and transactions of the Puerto Rico Department of Health in conformity with the accounting principles generally accepted in the United States of America.

Other Matters

Restatement

As discussed in Note 17 to the financial statements, subsequent to the issuance of the 2016 financial statements, the Employee Retirement System (ERS) of the Commonwealth of Puerto Rico provided the information needed to adopt the Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions,* an amendment of GASB Statement No. 27, and GASB Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date,* an amendment of GASB Statement No. 68, as of July 1, 2014. Accordingly, the financial statements as of and for the years ended June 30, 2016 and 2015 have been restated to report the results of the adoption of these pronouncements. Our opinion is not modified with respect to this matter.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis information on pages 1 to 14 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated August 9, 2017 on our consideration of the Administration's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Administration's internal control over financial reporting and compliance.

San Juan, Puerto Rico
August 9, 2017 (except as to Notes 9, 17, 18, which are
as of November 15, 2018)

Puerto Rico Medical Services Administration
A Component Unit of the Puerto Rico Department of Health

Statements of Net Position

June 30, 2016 and 2015

	2016 (As restated)	2015 (As restated)
Assets		
Current assets:		
Cash in commercial banks	$ 559,627	$ 1,754,490
Accounts receivable:		
Member institutions, net	33,674,828	21,658,796
Private insurance, net	15,812,843	18,085,649
Note receivable from Municipality of San Juan	850,000	800,000
Other, net	57,863	48,166
Inventories	3,568,009	3,556,922
Prepaid expenses	510,276	489,027
Total current assets	55,033,446	46,393,050
Non-current assets:		
Cash in commercial banks - restricted	3,337,764	1,165,948
Note receivable from Municipality of San Juan	1,850,000	2,700,000
Due from Commonwealth of Puerto Rico	-	13,144,646
Capital assets, net	56,281,514	59,413,058
Total non-current assets	61,469,278	76,423,652
Total assets	116,502,724	122,816,702
Deferred outflows of resources - pension related	121,732,152	85,861,718
Liabilities and Net Position (Deficit)		
Current liabilities:		
Accounts payable and accrued expenses	88,423,330	78,608,021
Accrued interest	30,091,487	13,144,646
Current portion of accrued pension costs	71,159,639	48,030,408
Current portion of compensated absences	9,255,716	7,428,475
Liabilities payable from restricted assets - improvements to medical facil	455,912	661,407
Total current liabilities	199,386,084	147,872,957
Non-current liabilities:		
Line of credit	282,447,692	282,445,142
Net pension liability	609,076,916	504,172,660
Accrued pension costs, net of current portion	-	1,022,638
Compensated absences, net of current portion	5,866,988	5,078,456
Other post-employment benefit obligations	1,834,301	1,834,301
Liabilities payable from restricted assets - Self-insurance fund	2,300,000	2,444,227
Total non-current liabilities	901,525,897	796,997,424
Total liabilities	1,100,911,981	944,870,381
Deferred inflows of resources - pension related	10,565,214	3,185,505
Net position:		
Net invested in capital assets	56,281,514	59,413,058
Restricted for permanent improvements	93,640	-
Restricted for others	535,525	535,142
Unrestricted (deficit)	(930,152,998)	(799,325,666)
Total net position (deficit)	$ (873,242,319)	$(739,377,466)

See notes to financial statements

Puerto Rico Medical Services Administration
A Component Unit of the Puerto Rico Department of Health

Statements of Revenues, Expenses and Changes in Net Position (Deficit)

For the years ended June 30, 2016 and 2015

	2016 (As restated)	2015 (As restated)
Patient service revenue, net of contractual allowances	$ 147,709,089	$ 153,217,200
Less: provision for bad debts	16,222,608	16,986,701
Net patient service revenue	131,486,481	136,230,499
Operating costs and expenses:		
Cost of services	161,435,831	158,722,178
General and administrative	14,667,739	15,316,041
Depreciation and amortization	5,054,115	4,973,616
Provision for bad debts	13,144,646	-
Pension expense	76,413,531	26,198,423
Total operating cost and expenses	270,715,862	205,210,258
Operating loss	(139,229,381)	(68,979,759)
Non-operating revenue (expenses):		
Contributions from the Commonwealth of Puerto Rico	27,769,613	46,609,462
Other (loss) / income	(23,220)	638,327
Loss on disposition of capital assets	(3,378)	(25,131)
Interest expense	(22,378,487)	(19,996,465)
Total non-operating revenue, net	5,364,528	27,226,193
Net change in net position	(133,864,853)	(41,753,566)
Net position (deficit), at beginning of year	(739,377,466)	(697,623,900)
Net position (deficit), at end of year	$ (873,242,319)	$ (739,377,466)

See notes to financial statements

Puerto Rico Medical Services Administration
A Component Unit of the Puerto Rico Department of Health

Statements of Cash Flows

For the years ended June 30, 2016 and 2015

	2016 (As restated)	2015 (As restated)
Cash flows from operating activities:		
Receipts from service revenues	$ 122,533,557	$ 131,522,520
Payments to suppliers for goods and services and, salaries and related benefits	(141,947,953)	(153,362,280)
Net cash used in operating activities	(19,414,396)	(21,839,760)
Cash flows from non capital and related financing activities:		
Intergovernmental contributions	27,759,747	46,308,472
Interest paid	(5,431,646)	(19,996,465)
Net cash provided by non capital and related financing activities	22,328,101	26,312,007
Cash flows from capital and related financing activities:		
Intergovernmental contributions	9,866	300,990
Acquisition of machinery and equipment	(1,102,827)	(1,823,547)
Improvements to emergency room and other facilities	(823,121)	(2,722,750)
Borrowings under line of credit	2,550	-
Net cash used in capital and related financing activities	(1,913,532)	(4,245,307)
Cash flows from investing activities:		
Change in restricted cash	(2,171,816)	(209,032)
Receipts from interest and other income	(23,220)	638,327
Net cash (used in) provided by investing activities	(2,195,036)	429,295
Net change in cash	(1,194,863)	656,235
Unrestricted cash, beginning of year	1,754,490	1,098,255
Unrestricted cash, end of year	$ 559,627	$ 1,754,490

(Continues)

Puerto Rico Medical Services Administration
A Component Unit of the Puerto Rico Department of Health

Statements of Cash Flows (Continued)

For the years ended June 30, 2016 and 2015

	2016 (As restated)	2015 (As restated)
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$ (139,229,381)	$ (68,979,759)
Adjustments to reconcile operating loss to net cash used in operating activities		
Depreciation and amortization	5,054,115	4,973,616
Provision for bad debts	29,367,254	16,986,701
Write down of prepaid expenses	-	194,824
Changes in assets and liabilities		
(Increase) decrease in:		
Accounts receivable	(25,175,532)	(21,694,680)
Inventories	(11,087)	(87,833)
Prepaid expenses	(21,250)	167,799
Deferred outflows of resources - pension related	(35,870,434)	(85,861,718)
Increase (decrease) in:		
Accounts payable	10,909,307	7,194,592
Accrued expenses and other	23,278,647	13,206,557
Net pension liability	104,904,256	108,874,636
Deferred inflows of resources - pension related	7,379,709	3,185,505
	119,814,985	47,139,999
Net cash used in operating activities	$ (19,414,396)	$ (21,839,760)

Non-cash capital investing and financing activities

	2016	2015
Retirement of capital assets	$ 187,084	$ 671,066
Payments to suppliers with proceeds from line of credit	$ -	$ 4,153,358
Intergovernmental contribution for the payment of interest expenses	$ -	$ 13,144,646

See notes to financial statements

Note 1 - Organization and summary of significant accounting policies

Organization

The Puerto Rico Medical Services Administration (the Administration), is a public corporation and an instrumentality of the Commonwealth of Puerto Rico (the Commonwealth) adhered to the Puerto Rico Department of Health (the Department). The Administration was created by Law Number 66 of June 22, 1978, as amended, to plan, organize, operate and administer the centralized health services, provided in support of hospitals and other functions offered by the member institutions and consumers of the complex known as Puerto Rico Medical Center. As a component unit of the Department, the Administration is also included as part of the Department's reporting entity.

As an instrumentality of the Commonwealth, the Administration is exempt from income, property and municipal license tax.

The Administration's capital is funded by non-reimbursable legislature appropriations from the Commonwealth, in-kind donations or cash from various governmental agencies or instrumentalities of the Commonwealth, federal grants and other contributions.

Summary of significant policies

The accounting and reporting policies of the Administration conform to accounting principles generally accepted in the United States of America, as applicable to governmental units. The following is a description of the most significant accounting policies:

Basis of presentation

The Administration's financial statements are presented as an enterprise fund and conform to the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34 (GASB No. 34), *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments.* GASB 34, as amended, establishes standards for external financial reporting for all state and local government entities, which includes a statement of net position, a statement of revenues, expenses and changes in net position, and a statement of cash flows. It requires the classification of net assets into three components: net invested in capital assets, restricted, and unrestricted.

Note 1 - Organization and summary of significant accounting policies - (continued)

Summary of significant policies – (continued)

Basis of presentation – (continued)

These classifications are defined as follows:

- Net invested in capital assets – This component of net assets consists of capital assets, net of accumulated depreciation, reduced by outstanding balances of any bonds, mortgage notes, or other borrowings that are attributable to and spent in the acquisition, construction, or improvement of those assets.

  If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of net invested in capital assets; rather, that portion of the debt is included in the same net assets component as the unspent proceeds. As of June 30, 2016 and 2015, net assets invested in capital assets, net of related debt consisted of the balance of capital.

- Restricted – This component of net assets consists of constraints placed on net assets use through external constraints imposed by creditors (such as through debt covenants), contributions, or laws or regulations of other governments of constraints imposed by law through constitutional provisions or enabling legislation. As of June 30, 2016 and 2015, net assets restricted consisted mainly of cash available from governmental contributions received for improvements to the Administration's facilities and other capital additions.

- Unrestricted deficit – This component of net assets consists of net assets that do not meet the definition of "restricted" or "net invested in capital assets".

Measurement focus and basis of accounting

The financial statements of the Administration are presented using the economic resources measurement focus and the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America, as applicable to governmental units. Under this basis, revenues are recognized when earned, regardless of when received, and expenses are recognized when incurred, regardless of when paid.

Note 1 - Organization and summary of significant accounting policies - (continued)

Summary of significant policies – (continued)

Use of estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, including estimated uncollectable for accounts receivable for services to patients, and liabilities, including estimated malpractice liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amount of revenue and expenses incurred during the reporting period. The reserve for doubtful accounts, and the estimated malpractice liabilities, among other accounts, require the significant use of estimates. Actual results could differ from those estimates.

Accounts receivable

Accounts receivable from member institutions are presented net of advances received by the Administration from these institutions. These advances are received on a quarterly basis and are applied to the accounts receivable as services are rendered. As of June 30, 2016, approximately $60,460,606 and $140,392,010, representing receivables from member institutions and private insurance, respectively, are not expected to be collected, which are included as part of the allowance for doubtful accounts within accounts receivable in the accompanying statements of net position.

Valuation of accounts receivable

The Administration makes judgments as to the collectability of accounts receivables based on historical trends and future expectations. Management estimates an allowance for doubtful accounts, which represents the collectability of patient service accounts receivables.

This allowance adjusts gross patient service accounts receivable downward to their estimated net realizable value. To determine the allowance for doubtful accounts, management reviews specific customer risk for accounts over 365 days using the Administration's accounts receivable aging subsidiary.

Note 1 - Organization and summary of significant accounting Policies - (continued)

Summary of significant policies – (continued)

Fair value of financial instruments

The carrying amounts reported in the statement of net position for cash, receivables, other receivables, note receivable, line of credit, payables and accrued liabilities approximate their fair value due to their short-term duration.

Inventories

Inventory of supplies consisting of drugs, medicines, food and other supplies is stated at the lower of cost or net realizable value on the first-in, first-out basis.

Capital assets

Capital assets are stated at cost and equipment under capital leases at the present value of minimum lease payments, in accordance with the provision of the Financial Accounting Standards Board *FASB Accounting Standards Codification Topic of Accounting for Leases*. Capital assets are defined by the Administration as assets with an individual cost of more than $100.

Depreciation and amortization are computed using the straight-line method over the estimated useful life of the related assets or the lease term, as follows:

Description	Useful Life
Land improvements	40 years
Building	40 years
Building improvements	5 years
Machinery and equipment	3-20 years
Equipment under capital leases	Lease term (useful live or lease term, whichever is shorter)

At the time capital assets are sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the Administration's books and the resulting gain or loss, if any, is credited or charged to operations.

Note 1 - Organization and summary of significant accounting policies - (continued)

Summary of significant policies – (continued)

Accounting for the impairment of capital assets

The Administration accounts for assets impairment under the provisions of GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries.* This statement establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its services utility has declined significantly and unexpectedly. This statement also establishes accounting requirements for insurance recoveries. A capital asset generally should be considered impaired if both, (a) the decline in service utility of the capital asset is large in magnitude, and (b) the event of change in circumstance is outside the normal life cycle of the capital asset. Impaired capital assets that will no longer be used by the government should be reported at the lower of carrying value or fair value.

Compensated absences

The vacation and sick policy of the Administration provides for the accumulation of thirty (30) days of vacation and eighteen (18) days of sick leave annually. Vacation time is fully vested to the employees from the first day of work. Under the collective bargain agreement, which went into effect on January 1, 2013, employees are entitled to the payment of the excess of sixty (60) days of vacation at a rate equal to double of their hourly rate. On the other hand, employees not covered under the collective bargain agreement are entitled to the payment of the excess of sixty (60) days of vacation at their hourly rate. However, as per Law No. 66 of June 17, 2014, payment of the excess of sixty (60) days of vacation cannot be completed for employees not covered under the collective bargain agreement.

Under the collective bargain agreement and the Administration policies, all employees are entitled to the payment of the excess of fifteen (15) days in accumulated sick leave, up to a maximum of eighteen (18) days. However, as per Law No. 66 of June 17, 2014, and the collective bargain agreement required by it, the payment previously mentioned cannot be completed for employees not covered under the collective bargain agreement.

Note 1 - Organization and summary of significant accounting policies - (continued)

Summary of significant policies – (continued)

Net patient service revenue

The Administration has agreements with third-party payors that provide for payments to the Administration at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursement costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

The Administration follows the requirements of the FASB Accounting Standards Update No. 2011-07, *Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts and the Allowance for Doubtful Accounts for Certain Healthcare Entities.* The standard update requires healthcare entities that recognize a significant amount of patient service revenue at the time the services are rendered, even though they do not assess the patient's ability to pay at that moment, to present as a separate line item on the face of the statement of revenues, expenses and changes in net position, the provision for bad debts, related to patient service revenue, as a deduction from patient revenue (net of contractual allowances and discounts).

The standard update also requires disclosing by major payor source of revenue; the Administration's policy for assessing collectability in determining the timing and amount of patient service revenue to be recognized, and qualitative and quantitative information about significant changes in the allowance for doubtful accounts related to patient accounts receivable.

This Space Is Intentionally Left In Blank

Note 1 - Organization and summary of significant accounting policies - (continued)

Summary of significant policies – (continued)

Post-employment benefits other than pension benefits

The Administration adopted the provisions of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions.* The Administration provides post-retirement benefits to all employees who meet certain age and years of services requirements. Such benefits consist principally of health care benefits and a post-employment payment. Healthcare benefits are provided for a period of six (6) months after retirement. A lump-sum payment is made for post-employment bonus after retirement. However, as per Law No. 66 of June 17, 2014, employees not covered under the collective bargain agreement will not receive the post-employment bonus after retirement. Substantially, all the Administration's employees may become eligible for those benefits if they reach normal retirement age while working for the Administration.

Revenues

Consist primarily of services provided to member institutions, third party payors, others, and are reported at the estimated net realizable amounts for services rendered to patients.

Operating revenues and expenses

Operating revenues and expenses are those that result from operating service activities. Interest income and expenses related mainly with restricted deposits, obligations under capital leases and other are not included as part of operating revenues and expenses.

Insurance

The Administration carries commercial insurance to cover for casualty, theft, claims and other losses. The Commonwealth negotiates the commercial insurance coverage, and the cost is paid by the Administration. The Administration is self-insured for medical malpractice claims and judgments, as discussed in Note 6. The Administration also pays for workers' compensation insurance to another component unit of the Commonwealth.

Note 1 - Organization and summary of significant accounting policies - (continued)

Summary of significant policies – (continued)

Non-exchange transactions

GASB Statement No. 33, *Accounting and Financial Reporting for Non-exchange Transactions*, establishes accounting and financial reporting standards for non-exchange transactions involving financial or capital resources (for example, grants, and contributions). In a non-exchange transaction, a government gives (or receives) value without directly receiving (or giving) equal value in return. This is different from an exchange transaction, in which each party receives and gives up essentially equal value. Under the provisions of the GASB 33, the provider and the recipient should recognize the non-exchange transaction as an expense and revenue, respectively, when all eligibility requirements are satisfied.

Deposits and investment risks

The Administration follows the GASB Statement No. 40, *Deposit and Investment Risk Disclosure* – an amendment of GASB Statement No. 3. The Statement addresses common deposit and investment risks related to credit, concentration, interest rate and foreign currency. Among other disclosures, the Statement requires certain disclosures applicable to deposits or investments having fair values that are highly sensitive to changes in interest rate.

Deferred outflows and inflows of resources

The Administration adopted GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which requires that, in addition to assets, the statement of net position will sometimes report a separate section of deferred outflows of resources, which represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. Also, in addition to liabilities, the statement of net position will sometimes report a separate section of deferred inflows of resources, which represents an acquisition 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, 2016 and 2015, all deferred outflows of resources and all deferred inflows of resources of the Administration are pension related items, as further disclosed in Note 9.

Note 1 - Organization and summary of significant accounting policies - (continued)

Reclassifications

Certain reclassifications have been made to the 2015 financial statements to conform them to the 2016 financial statements presentation.

New accounting standards adopted

The Administration accounts for pension costs under the provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, an amendment of GASB Statement No. 27, and GASB Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date*, an amendment of GASB Statement No. 68, which were adopted effective July 1, 2014 in the accompanying financial statements. GASB Statement No. 68 replaced GASB Statement No. 27 and requires that employers report a net pension liability and related pension accounts, such as pension expense and deferred outflows/inflows of resources as determined by the Employees Retirement Systems (ERS), as applicable, under the requirements contained in GASB Statement No. 67, *Financial Reporting for Pension Plans* – an amendment of GASB Statement No. 25.

The major fundamental change brought by GASB Statement No. 67, was switching from the then 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; to an "accrual basis" model, where the total pension obligation (actuarially determined) is compared to the plan net position and the difference represents the net pension liability. The Primary Government of the Commonwealth of Puerto Rico, as well as its component units and the municipalities, are considered "cost sharing" employers of the ERS; therefore, the Administration reports its allocated share of the ERS's net pension liability and the related pension amounts.

The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments (GASB No. 76) - The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The "GAAP hierarchy" consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. This pronouncement is effective for fiscal year June 30, 2016.

Note 1 - <u>Organization and summary of significant accounting policies - (continued)</u>

<u>Accounting pronouncements issued but not yet effective</u>

The following summarizes new accounting standards that have been issued but are not yet effective, which are expected to have a direct and material effect on the Administration's financial statements once they become effective:

Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68 (GASB No. 73) - This Statement establishes requirements for defined benefit pensions that are not within the scope of Statement No. 68, Accounting and Financial Reporting for Pensions, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement 68. It also amends certain provisions of Statement No. 67, Financial Reporting for Pension Plans, and Statement 68 for pension plans and pensions that are within their respective scopes. The requirements of this Statement extend the approach to accounting and financial reporting established in Statement 68 to all pensions, with modifications as necessary to reflect that for accounting and financial reporting purposes, any assets accumulated for pensions that are provided through pension plans that are not administered through trusts that meet the criteria specified in Statement 68 should not be considered pension plan assets.

It also requires that information similar to that required by Statement 68 be included in notes to financial statements and required supplementary information by all similarly situated employers and non-employer contributing entities. This Statement also clarifies the application of certain provisions of Statements 67 and 68 with regard to the following issues:

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

Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (GASB No. 75) - The scope of this Statement addresses accounting and financial reporting for OPEB that are provided to the employees of state and local governmental employers. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments,

Note 1 - Organization and summary of significant accounting policies - (continued)

Accounting pronouncements issued but not yet effective – (continued)

Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (GASB No. 75) – (continued)

discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed. The requirements of this Statement are effective for financial statements for reporting periods beginning after June 15, 2017.

Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73 (GASB No. 82) - The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. 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 of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The requirements of this Statement are effective for financial statements for reporting periods beginning after June 15, 2016.

Additional accounting pronouncements have been issued and are not yet effective.

The impact of these statements on the Administration's basic financial statements has not yet been determined.

This Space Is Intentionally Left In Blank

Note 2 - Cash in commercial banks - restricted

Cash in commercial banks - restricted as of June 30, 2016 and 2015 consisted of:

Description	2016	2015
Cash-restricted for:		
Improvements to medical facilities		
and purchase of equipment	$ 543,716	$ 397,212
Self-insurance fund	2,257,327	232,397
Gamma Knife	2,592	2,210
Other	534,129	534,129
	$ 3,337,764	$ 1,165,948

The Administration's restricted cash are comprised of deposits held in custody by a banking institution. These deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to $250,000, with the remaining balance collateralized with financial instruments held by a trust of the Commonwealth. Based on these provisions, deposits are not considered to be subject to custodial credit risk, which is the risk that in the event of a bank's failure, the Administration's deposits may not be returned.

Note 3 - Net patient service revenue

The Administration has agreements with medical insurance companies, governmental entities of the Commonwealth of Puerto Rico and the Medicare program for payments to the Administration, at amounts different from its established rates. A summary of the most significant agreements, with these entities is as follows:

Medicare - Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient capital costs are paid based on the fully prospective method. Medical education costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The Administration is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of an annual cost report by the Administration and audits thereof by the Medicare fiscal intermediary.

The Administration's Medicare cost reports have been reviewed by the Medicare fiscal intermediary through 2013.

Note 3 - Net patient service revenue – (continued)

The cost reports from 2014 to 2016 are subject to the Medicare fiscal intermediary examination. Laws and regulations governing the Medicare program are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term.

Member institutions – The Administration has agreements with different governmental entities of the Commonwealth of Puerto Rico for payments to the Administration, at its established rates.

Others – Also, the Administration has entered into payment agreements with some commercial insurance carriers and other healthcare organizations. The basis for payment to the Administration under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

A summary of patient service revenue, net of contractual allowances and discounts, and provision for bad debts, for the years ended June 30, 2016 and 2015 consisted of:

	2016	2015
Third-party payors - member institutions	$ 97,778,514	$ 96,078,896
Third-party payors - health plans	33,757,904	40,152,088
Self-pay patients	(49,937)	(485)
Patient service revenue (net of contractual allowances and discounts and provision for bad debts)	$ 131,486,481	$ 136,230,499

Changes in the allowance for doubtful accounts on patient's account receivable for the years ended June 30, 2016 and 2015 consisted of:

	2016	2015
Balance, beginning of year	$ 192,847,346	$ 180,018,997
Provision for bad debts	16,222,608	16,986,701
Write-off of uncollectible accounts	(8,217,338)	(4,158,352)
Balance, end of year	$ 200,852,616	$ 192,847,346

Note 3 - Net patient service revenue – (continued)

Net patient service revenue from third-party payors is estimated fully collectible and it is recorded when the health care services are provided. Also, health care services provided to uninsured patients are recorded when the services are provided. Provision for bad debts related to receivables from third-party payors and uninsured patients and for patients for whom it was assessed the patient does not has the ability to pay is recorded as a deduction of net patient service revenue in the accompanying statements of revenues, expenses and changes in net position. At June 30, 2016 and 2015, 74% and 75%, respectively, of the amounts reserved as uncollectible are related to third-party payors, 26% and 25%, respectively, are related to self-pay patients, which includes deductibles and co-insurance which the Administration accounts for as patient balance.

This Space Is Intentionally Left In Blank

Note 4 - Capital assets

Capital assets as of June 30, 2016 and 2015, and activity during the years then ended consisted of:

Description	Balance June 30, 2015	Acquisitions	Retirements	Balance June 30, 2016
Capital assets not being depreciated:				
Land	$ 6,871,955	$ -	$ -	$ 6,871,955
Capital assets being depreciated:				
Land improvements	11,916,569	-	-	11,916,569
Building and improvements	93,973,503	728,605	-	94,702,108
Machinery and equipment	57,626,404	1,102,827	(187,084)	58,542,147
Equipment under capital leases	18,435,727	-	-	18,435,727
	181,952,203	1,831,432	(187,084)	183,596,551
Accumulated depreciation and amortization:				
Land improvements	11,877,232	9,834	-	11,887,066
Building and improvements	53,936,311	2,211,823	(94,836)	56,053,298
Machinery and equipment	45,161,829	2,832,458	(183,387)	47,810,900
Equipment under capital leases	18,435,728	-	-	18,435,728
	129,411,100	5,054,115	(278,223)	134,186,992
Capital assets being depreciated, net	52,541,103	(3,222,683)	91,139	49,409,559
Capital assets, net	$ 59,413,058	$ (3,222,683)	$ 91,139	$ 56,281,514

Note 4 - Capital assets – (continued)

Description	Balance June 30, 2014	Acquisitions	Retirements	Balance June 30, 2015
Capital assets not being depreciated:				
Land	$ 6,871,955	$ -	$ -	$ 6,871,955
Capital assets being depreciated:				
Land improvements	11,867,399	49,170	-	11,916,569
Building and improvements	91,261,116	2,712,387	-	93,973,503
Machinery and equipment	56,453,320	1,784,722	(611,638)	57,626,404
Equipment under capital leases	18,456,330	-	(20,603)	18,435,727
	178,038,165	4,546,279	(632,241)	181,952,203
Accumulated depreciation and amortization:				
Land improvements	11,854,398	22,834	-	11,877,232
Building and improvements	51,771,461	2,164,850	-	53,936,311
Machinery and equipment	42,962,422	2,785,932	(586,525)	45,161,829
Equipment under capital leases	18,456,331	-	(20,603)	18,435,728
	125,044,612	4,973,616	(607,128)	129,411,100
Capital assets being depreciated, net	52,993,553	(427,337)	(25,113)	52,541,103
Capital assets, net	$ 59,865,508	$ (427,337)	$ (25,113)	$ 59,413,058

Note 5 - Note receivable from the Municipality of San Juan

On November 14, 2013 the Administration and the Municipality of San Juan (MSJ) signed an agreement to settle the accounts receivable from the Hospital of the Municipality of San Juan related to medical services rendered by the Administration to the MSJ covering inpatient and outpatient services, laboratory, pharmacy, general services and other ancillary services billed to the MSJ. The settlement was for the amount of $11,500,000 and covers the period from July 1, 2002 to June 30, 2012. The agreement is to be paid in five installments beginning in fiscal year 2014 for $8 million, $800,000 in 2016, $850,000 in 2017, $900,000 in 2018 and the last payment is due August 2019 for $950,000, bearing no interest.

Note 6 - Self-insurance fund

Beginning in fiscal year 1986, the Administration decided to stop carrying commercial insurance because of its prohibitive cost and approved the establishment of a Self-Insurance Fund (the Fund) to account for and finance its uninsured risks of loss related to professional liability claims. Patient and non-patient general liability exposures are insured elsewhere and are not covered by the Fund.

The Administration maintains in the Fund cash of $2,257,327 and $232,397 as of June 30, 2016 and 2015, respectively, to provide for the payment of possible claims. Funding requirements are determined based on actuarial reports and the Administration's Internal Council Office. The most recent actuarial reports as of June 30, 2016 and 2015, presented estimated liabilities of approximately $2,300,000 and $2,444,227, respectively, which were related to claims incurred during the years ended June 30, 1989 to June 30, 2016.

The following is the activity of the restricted cash available and liabilities payable from restricted assets under the Self-Insurance Fund for the years ended June 30, 2016 and 2015.

June 30, 2016:

Description	Restricted Cash	Liabilities Payable
Balances as of beginning of year	$ 232,397	$ 2,444,227
Funds received from operations	10,191,807	18,050
Claims paid and other disbursements	(8,166,877)	(162,277)
Balance as of end of year	$ 2,257,327	$ 2,300,000

June 30, 2015:

Description	Restricted Cash	Liabilities Payable
Balances as of beginning of year	$ 39,956	$ 2,800,000
Funds received from operations	580,212	-
Claims paid and other disbursements	(387,771)	(355,773)
Balance as of end of year	$ 232,397	$ 2,444,227

Note 7 - Accrued pension costs

Accrued pension costs as of June 30, 2016 and 2015 consisted of:

June 30, 2016:

Description	Amount
Employer's contributions	$ 21,800,897
Employee's contributions	11,644,114
Employee's and employer's contributions under System 2000	5,340,596
Withholdings of employees' loans	1,934,381
Interest and other	30,439,651
	71,159,639
Less: current portion	(71,159,639)
Accrued pension cost, net of current portion	$ -

June 30, 2015:

Description	Amount
Employer's contributions	$ 13,513,184
Employee's contributions	7,345,339
Employee's and employer's contributions under System 2000	4,338,468
Withholdings of employees' loans	1,613,294
Interest and other	22,242,761
	49,053,046
Less: current portion	(48,030,408)
Accrued pension cost, net of current portion	$ 1,022,638

This Space Is Intentionally Left In Blank

Note 7 - Accrued pension costs (continued)

On November 1, 2011, the Administration entered into a payment plan agreement (the Agreement) with the Administration of the Employee's Retirement System of the Government of the Commonwealth of Puerto Rico for repayment of a debt amounting to $15,340,620, at such date, corresponding to fiscal year 2010-2011. Beginning on November 15, 2011, the agreement calls for sixty (60) monthly installments of $255,677 bearing no interest. Default payments of less than one year in default, will bear interest at 9%, and 12% for those in excess of one year. No payment plan has been agreed to for the repayment of the debt amounting to $71 million from fiscal years from 2012 to 2016.

Note 8 - Employees' retirement plan

Retirement System

The Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (the Retirement System), created pursuant to Act No. 447 of May 15, 1951, as amended, is a cost-sharing, multiple-employer, defined benefit pension plan sponsored by and reported as a component unit of the Commonwealth. The Retirement System consists of different benefit structures, including a cost-sharing, multi-employer, defined benefit program, a defined contribution program (System 2000 Program) and a defined contribution hybrid program.

Defined Benefit Program

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

The Defined Benefit Program provides retirement, death, and disability benefits pursuant to legislation enacted by the Legislature. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after 10 years of plan participation. Disability benefits are available to members for occupational and non-occupational disabilities. However, a member must have at least 10 years of service to receive non-occupational disability benefits.

Note 8 - Employees' retirement plan – (continued)

Defined Benefit Program – (continued)

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

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

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

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

On September 24, 1999, the Legislature enacted Act No. 305 which amended Act No. 447 to establish a new retirement program (System 2000 Program). In addition, on April 4, 2013, the Legislature enacted Act No. 3 which amended the provisions of the different benefit structures under the Retirement System, including the Defined Benefit Program.

Note 8 - Employees' retirement plan – (continued)

System 2000 Program

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

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

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

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

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

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

Note 8 - Employees' retirement plan – (continued)

Defined Contribution Hybrid Program

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

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

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

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

1. Increased the minimum pension for current retirees from $400 to $500 per month.
2. The retirement age for the Act No. 447 participants will be gradually increased from age 58 to age 61.
3. The retirement age for the active System 2000 Program participants will be gradually increased from age 60 to age 65.

Note 8 - Employees' retirement plan – (continued)

Defined Contribution Hybrid Program – (continued)

4. Eliminated the "Merit Annuity" available to participants who joined the Retirement System prior to April 1, 1990.
5. The retirement age for new employees was increased to age 67.
6. The employee contribution rate was increased from 8.275% to 10%.
7. For the System 2000 Program participants, the retirement benefits will no longer be paid as a lump sum distribution, instead, they will be paid through a lifetime annuity.
8. Eliminated or reduced various retirement benefits previously granted by special laws, including Christmas and summer bonuses. The Christmas bonus payable to current retirees was reduced from $600 to $200 and was eliminated for future retirees. The summer bonus was eliminated. Resulting employer contribution savings will be contributed to the Retirement System.
9. Disability benefits were eliminated and substituted for a mandatory disability insurance policy.
10. Survivor benefits were modified.

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

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

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

Note 8 - Employees' retirement plan – (continued)

Defined Contribution Hybrid Program – (continued)

Total employee required contributions for the Defined Contribution Hybrid Program during the year ended June 30, 2016, amounted to $8,324,411. The Administration required contributions during the years ended June 30, 2016, 2015 and 2014 amounted to $8,633,929, $8,194,019, and $7,523,631, respectively. These amounts represented 100% of the required contribution for the corresponding year. Individual information for each option is not available since the allocation is performed by the Retirement System itself.

Additional information on the Retirement System is provided on its standalone financial statements for the year ended June 30, 2015, a copy of which can be obtained from the Employees' Retirement System of the Commonwealth of Puerto Rico, P.O. Box 42004, San Juan PR 00940-2004.

As of June 30, 2016 and 2015, the total unpaid employee and employer contributions, due to the Retirement System including interest, amounted to $71,159,639 and $49,053,046.

Note 9 - Net pension liability

The Commonwealth's net pension liability, from which an allocation was made to the Administration's financial statements as of June 30, 2016 and 2015, was measured as of June 30, 2015 and 2014, respectively, and the total pension liability used to calculate the net pension liability was determined by actuarial valuations with beginning of years census data as of July 1, 2014 and 2013, respectively, that was updated to roll forward the total pension liability to June 30, 2015 and 2014, respectively, assuming no gains or losses.

Actuarial methods and assumptions

The following actuarial methods and assumptions were used in developing the estimate of the net pension liability of the Commonwealth of Puerto Rico's Retirement System, from which an allocation of the net pension liability was made for the Administration and other instrumentalities of the Commonwealth of Puerto Rico.

This Space Is Intentionally Left In Blank

Note 9 - Net pension liability – (continued)

Actuarial methods and assumptions – (continued)

The total pension liabilities in the June 30, 2015 and 2014 actuarial valuations were determined using the following actuarial methods and assumptions, applied to all periods included in the measurement:

	Actuarial valuations as of: June 30, 2015	Actuarial valuations as of: June 30, 2014
Actuarial cost method	Entry age normal	Entry age normal
Asset-valuation method	Market value of assets	Market value of assets
Actuarial assumptions:		
Inflation	2.5%	2.5%
Investment rate of return, net of investment expenses, including inflation	6.5	6.8
Municipal bond index	3.8	4.3
Discount rate	3.8	4.3
Projected salary increases per annum	3.0% per annum. No compensation increases are assumed until July 1, 2017 as a result of Act No. 66 and the current general economy.	3.0% per annum. No compensation increases are assumed until July 1, 2017 as a result of Act No. 66 and the current general economy.
Cost-of-living adjustments	None assumed.	None assumed.

The mortality tables used in the June 30, 2015 actuarial valuations were as follows:

- Pre-retirement Mortality – For general employees not covered under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement Scale MP-2015 from the 2006 base year and projected forward using MP-2015 on generational basis. For members covered under Act No. 127, RP-2014 Employee Mortality Rates are assumed with blue collar adjustments for males and females adjusted to reflect Mortality Improvement Scale MP-2015 from the 2006 base year and projected forward using MP-2015 on generational basis. As generational tables, they reflect mortality improvements both before and after the measurement date. Also, 100% of deaths while in active service are assumed to be occupational only for members covered under Act No. 127.

- Post-retirement health mortality: rates, which vary by gender, are assumed for healthy retirees and beneficiaries based on a study of the plan's experience from 2007 to 2012 equal to 92% of the rates from the Uninsured Pensioner (UP) 1994 Mortality Table for Males and 95% of the rates from the UP 1994 Mortality Table for Females. The rates are projected on a generational basis starting in 1994 using Scale AA. As a generational table, it reflects mortality improvements for both before and after the measurement date.

Note 9 - Net pension liability – (continued)

Actuarial methods and assumptions – (continued)

- Post-retirement disabled mortality: rates, which vary by gender, are assumed for disabled retirees based on a study of the plan's experience from 2007 to 2012 equal to 105% of the rates from the UP 1994 Mortality Table for Males and 115% of the rates from the UP-Mortality Table for Females. No provision was made for future mortality improvement for disabled retirees.

The mortality tables used in the June 30, 2014 actuarial valuations were as follows:

- Pre-retirement mortality: for employees not covered under Act No. 127 of June 10, 1967, mortality rates are assumed for males and females projected on a generational basis using Scale AA. For members covered under Act No. 127 of June 10, 1967, employee mortality rates are assumed with blue collar adjustments for males and females, projected on a generational basis using Scale AA. As generational tables, they reflect mortality improvements both before and after the measurement date. Also, 100% of the deaths while in active service are assumed to be occupational only for members covered under Act. No. 127.

The mortality tables used in the June 30, 2014 actuarial valuations for post-retirement health mortality and post-retirement disabled mortality are the same for those used in the June 30, 2015 actuarial valuations.

Long-term rate of return on investments

The long-term expected rate of return on pension benefit investments was determined in accordance with the portfolio asset allocation adopted by the corresponding boards of Retirement Systems during December 2013 and the actuary's capital market assumptions as of June 30, 2015 and 2014. In addition, the assumption reflects that loans to members comprise approximately 20% of the portfolio and, have an approximate return of 9.1% with no volatility. The long-term expected rate of return on pension benefit investments as of June 30, 2015 and 2014 was 6.55% and 6.75%, respectively. The long-term expected rate of return on pension benefit investments as of June 30, 2015 was equal to the highest debt service of the senior pension funding bonds payable, which ranged from 5.85% to 6.55% as of June 30, 2015. Also, as of June 30, 2014, the long-term expected rate of return on pension benefit investments was slightly higher than the debt service of the senior pension funding bonds payable, which also ranged from 5.85% to 6.55% as of June 30, 2014.

Note 9 - Net pension liability – (continued)

Long-term rate of return on investments – (continued)

The Retirement Systems' policies in regard to allocation of invested assets is established and may be amended by the corresponding Retirement System's Board. Plan assets are managed on a total return basis with a long-term objective of achieving and maintaining a positive impact on each of the Retirement Systems' financial condition for the benefits provided through the pension programs. The following are the Retirement System Board's adopted asset allocation policies as of June 30, 2015 and 2014:

		Long-term expected rate of return	
Asset class	Target allocation	June 30, 2015	June 30, 2014
Domestic equity	25%	6.4%	6.8%
International equity	10%	6.7%	7.6%
Fixed income	64%	6.3%	3.9%
Cash	1%	3.0%	2.9%
	100%		

The long-term expected rates of return on pension benefit investments were determined using a building block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) were developed for each major asset class. These ranges were 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.

Discount rate

The asset basis for the date of depletion projection is each of the Retirement Systems' fiduciary net position (the gross assets plus deferred outflows of resources less the gross liabilities, including the senior pension funding bonds payable, plus deferred inflows of resources). On this basis the Employees Retirement System fiduciary net position was expected to be exhausted during the fiscal year ended June 30, 2015. The projections assume that certain illiquid assets (consisting primarily of loans to members) of approximately $762 million and $764 million as of June 30, 2015 and 2014, respectively, will become converted to cash when needed. The discount rate used to measure the total pension liability decreased from 4.29% per annum in June 30, 2014 to 3.80% per annum in June 30, 2015.

Note 9 - Net pension liability – (continued)

Discount rate – (continued)

The fiduciary net position of the ERS was not projected to be available to make all projected future benefit payments of current active and inactive employees. The date of depletion projection in the actuarial report does not include any amounts from the additional uniform contribution required by Act No. 32 because of actual fiscal and budgetary financial difficulties, continued budget deficits and liquidity risks of the Commonwealth and its municipalities, and the risk that the financial condition of the Commonwealth and its municipalities do not improve in the near term.

Therefore, the tax-free municipal bond index (Bond Buyer General Obligation 20 Bond Municipal Bond Index) was applied to all periods of projected benefits payments to determine the total pension liability. The discount rate for the ERS was 3.80% and 4.29% as of June 30, 2015 and 2014, respectively.

Actuarial assumptions are revised periodically to more closely reflect both actual and anticipated future experience. Due to the change in census collection date to the beginning of the fiscal year rather that the end of the fiscal year, demographic gain/loss during the year is limited to the difference between actual and expected benefit payments, which arise from differences in termination and retirement activity and mortality versus expectations.

The Administration's proportion of the net pension liability of the ERS

The Administration's proportionate share of the net pension liability of the ERS and the proportion percentage of the aggregate net pension liability of ERS allocated to the Administration as of June 30, 2015 and 2014 amounted to $609,076,916 and $504,172,660, respectively, and 1.82701% and 1.67283%, respectively.

The Administration's proportion of the ERS's net pension liability was based on the actual required contributions of each of the participating employers that reflect each employer's projected long-term contribution effort. The contributions that reflect each employer's projected long-term contribution effort included in the proportionate share calculation are: (1) Act No. 116 of 2010 statutory payroll-based contribution, (2) Act No. 3 of 2013 supplemental contribution, and (3) other special law contributions. Contributions from the Administration to the ERS of approximately $13,193,000 were required during the period subsequent to the measurement date or during the period ended June 30, 2016. Other contributions to ERS that do not reflect an employer's projected long-term contribution effort, such as contributions that separately finance specific liabilities of an individual employer to ERS (i.e. local employer early retirement incentives), were excluded from the proportionate share calculation.

Note 9 - Net pension liability – (continued)

The Administration's proportion of the net pension liability of the ERS – (continued)

In addition, Act No. 32 of 2013, Additional Uniform Contribution (AUC), which is a contribution that reflects each employer's projected long-term contribution effort, was excluded from the proportionate share calculation because its collectability from various employers, including the Commonwealth, is uncertain at this moment. This prevents an overallocation of GASB Statement No. 68 amounts to the employers who have paid their AUC (or are expected to do so) and an under-allocation of GASB Statement No. 68 amounts to the employers who have not paid their AUC (or are not expected to do so).

Actuarial assumptions are revised periodically to more closely reflect both actual and anticipated future experience. Due to the change in census collection date to the beginning of the fiscal year, rather than the end of the fiscal year, demographic gain/loss during the year is limited to the difference between actual and expected benefit payments, which arise from differences in termination and retirement activity and mortality versus expectations.

The components of the net pension liability of the Administration's proportionate share as of June 30, 2015 and 2014 (measurement dates) are as follows:

Administration's proportionate share of:	2015	2014
Proportion of the net pension liability	1.82701%	1.67283%
Total pension liability	$ 596,868,857	$ 505,521,146
Plan fiduciary net position (deficiency)	(12,208,059)	1,348,486
Net pension liability	$ 609,076,916	$ 504,172,660
Plan's fiduciary net position as a percentage of the total pension liability	-2.05%	0.27%
Covered payroll	$ 60,288,531	$ 61,837,502
Administration's proportionate share of the net pension liability as a percentage of its covered-employee payroll	9.90%	12.27%

The following table presents the Administration's proportionate share of the net pension liability as of June 30, 2015 for ERS calculated using the discount rate of 3.80%, as well as what the Administration's proportionate share of the net pension liability would be if it were calculated using a discount rate of 1% point lower (2.80%) or 1% point higher (4.80%) than the current rate:

Note 9 - Net pension liability – (continued)

The Administration's proportion of the net pension liability of the ERS – (continued)

	1% Decrease (2.80%)	Current Discount Rate (3.80%)	1% Increase (4.80%)
Administration's proportionate share of net pension liability	$ 694,346,235	$ 609,076,916	$ 539,214,743

The following table presents the Administration's proportionate share of the net pension liability as of June 30, 2014 for ERS calculated using the discount rate of 4.29%, as well as what the Administration's proportionate share of the net pension liability would be if it were calculated using a discount rate of 1% point lower (3.29%) or 1% point higher (5.29%) than the current rate:

	1% Decrease (3.29%)	Current Discount Rate (4.29%)	1% Increase (5.29%)
Administration's proportionate share of net pension liability	$ 571,960,249	$ 504,172,660	$ 448,036,033

Pension expense and deferred outflows of resources and deferred inflows of resources from pension activities

Pension expense recognized by the Administration for the years ended June 30, 2016 and 2015 related to the Retirement System amounts to $76,413,531 and $26,198,423, respectively.

This Space Is Intentionally Left In Blank

Note 9 - Net pension liability – (continued)

Pension expense and deferred outflows of resources and deferred inflows of resources from pension activities – (continued)

Deferred outflows and deferred inflows of resources from pension activities reported in the Administration's statements of net position as of June 30, 2016 and 2015 are as follows:

	Deferred outflows of resources	
	June 30, 2016	June 30, 2015
Differences between expected and actual experience in measuring total pension liability	$ 703,893	$ 773,394
Changes in assumptions	57,980,325	17,182,022
Changes in proportion and differences between actual contributions and proportionate share	49,854,599	56,656,392
Employer contributions made subsequent to the measurement date	13,193,335	11,249,910
	$ 121,732,152	$ 85,861,718

	Deferred inflows of resources	
	June 30, 2016	June 30, 2015
Net difference between projected and actual earnings on pension plan investments	$ 3,502,344	$ 3,185,505
Differences between expected and actual experience in measuring total pension liability	7,062,870	-
	$ 10,565,214	$ 3,185,505

This Space Is Intentionally Left In Blank

Note 9 - Net pension liability – (continued)

Amounts reported as deferred outflows/inflows of resources from pension activities as of June 30, 2016 will be recognized in the pension expense as follows:

Years ending June 30,	Amount
2017	$ 18,795,441
2018	18,795,441
2019	18,795,441
2020	20,566,358
2021	21,020,922
	$ 97,973,603

Deferred outflows of resources related to pensions resulting from the Administration's required contributions subsequent to the measurement date of June 30, 2015 amounted to $13,193,335 and will be recognized as a reduction of the net pension liability in the year ended June 30, 2017. This amount is not included in the table above.

Note 10 - Post-employment benefits - other than pensions

For the years ended June 30, 2016 and 2015, total covered payroll for employees was approximately $60,288,531 and $61,837,502, respectively. Covered payroll refers to all compensation paid by the Administration to employees covered by the Retirement System on which contributions to the pension are based.

Healthcare benefits

The Administration provides certain health care benefits (for a six-month period after retirement) and a post-employment bonus payment to eligible retired employees, financed on a pay-as-you-go basis. Substantially, all the Administration's employees may become eligible for those benefits if they reach normal retirement age while working for the Administration.

The Administration's annual other postemployment benefit (OPEB) cost (expense) for each plan is calculated based of the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty (30) years. The actuarial cost method used is the projected unit credit method.

Note 10 - Post-employment benefits other than pensions – (continued)

The calculation was based on the types of benefits provided under the terms of employees' collective bargain agreements. The calculation involves estimates of the value of reported amounts and assumptions about the probability of events far into the future, and such determined amounts are subject to continual revision as actual results compared to past experience and new estimates are made about the future. The required schedule of funding progress as of June 30, 2016, 2014, 2012 and 2010 presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

During fiscal year 2014 the health care benefits plan valuation determined in accordance with GASB 45 was segregated from the post-employment bonus plan, which valuation was performed in accordance with GASB 27 "Accounting for Pension by State and Local Government Employers". The actuaries allocated the June 30, 2012 benefits obligations between the healthcare benefit and the post-employment bonus based on their weight on the unfunded liability as of July 1, 2013.

Valuations are not conducted every year. Last full valuations were performed for the fiscal years beginning July 1, 2013 and July 1, 2016.

Healthcare benefits

Description	2016	2015
Benefit obligation, beginning of year	$ 1,673,113	$ 1,571,982
Benefit obligation related to GASB 27 reclassified	-	(176,250)
Change in benefit obligation:		
Annual required contribution	127,680	515,708
Interest on net OPEB obligation	15,889	55,829
Adjustment to annual required contribution	(34,357)	(89,344)
Benefits paid	(24,965)	(289,059)
Increase in net OPEB obligation	84,247	16,884
Benefit obligation accrued at end of year reflected in statement of net position	$ 1,757,360	$ 1,588,866

Note 10 - Post-employment benefits other than pensions – (continued)

Healthcare benefits – (continued)

	2016	2015
Assumptions:		
Discount rate	3%	4%
Expected long-term rate of return on plan assets	0%	0%
Health care cost trend rate:		
Initial	5.80%	6.80%
Ultimate	4.60%	4.60%
Retirement age	65 years	65 years

Required supplementary information

Schedule of Funding Progress ($ 000s)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Accrued Liability (b)	Unfunded Accrued Liability (UAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAL as a Percentage of Covered Payroll ((b-a)/c)
July 1, 2016	$ -	$2,888	$2,888	0.0%	$67,483	4.3%
July 1, 2013	$ -	$4,851	$4,851	0.0%	$72,326	6.7%
July 1, 2011	$ -	$4,676	$4,676	0.0%	$70,184	6.7%
July 1, 2009	$ -	$3,869	$3,869	0.0%	$72,395	5.3%

Schedule of Employer Contributions ($ 000s)

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
June 30, 2016	$328	22.9%	$1,841
June 30, 2014	$482	60.0%	$1,589
June 30, 2013	$472	60.0%	$1,589
June 30, 2012	$456	62.7%	$1,345

Note 10 - Post-employment benefits other than pensions – (continued)

Post-employment bonus plan

The Administration has collective bargain agreements that provide all union employees who work for the Administration upon retirement with a lump-sum bonus payable at the retirement date of $2,300 up to June 30, 2014. However, as per Law No. 66 of June 17, 2014, the bonus was reduced to $1,000 for the next three fiscal years, up to June 30, 2017. In addition, the non-union employees will not receive the post-employment bonus after retirement.

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

Funding Policy

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

The Administration's annual pension expense is calculated based on the ARC. The Administration engaged an actuary to calculate the ARC and related information per the provisions of GASB Statement No. 27 "Accounting for Pensions by State and Local Governmental Employers" (GASB 27) for employers with more than one hundred total plan members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Valuations are not conducted every year. Last full valuations were performed for the fiscal years beginning July 1, 2013 and July 1, 2016.

Note 10 - Post-employment benefits other than pensions – (continued)

Post-employment bonus plan – (continued)

The following table shows the Administration's annual pension cost and the amount actually contributed:

Description	2016	2015
Benefit obligation, beginning of year	$ 299,180	$ 176,250
Change in benefit obligation:		
Annual required contribution	74,338	78,847
Interest on net pension obligation	2,454	7,050
Adjustment to annual required contribution	(5,307)	(11,560)
Annual pension cost	71,485	74,337
Benefits paid	(17,741)	(5,152)
Increase in net pension obligation	53,744	69,185
Benefit obligation accrued at end of year reflected in statement of net position	$ 352,924	$ 245,435

Schedule of Employer Contributions ($000s)

Fiscal Year Ended	Annual Pension Cost	Percentage of Annual Pension Cost Contributed	Net Pension Obligation
June 30, 2016	$214	24.8%	$406
June 30, 2014	$74	6.9%	$245

The following assumptions were used to determine the annual required contributions of the benefit obligation as of June 30, 2016 and 2015:

	2016	2015
Discount rate	3.00%	4.00%
Mortality table	RP-2000	RP-2000

Note 10 - Post-employment benefits other than pensions – (continued)

Post-employment bonus plan – (continued)

As of June 30, 2016 and 2015 the actuarial accrued liability for benefits amount to approximately $2.2 million all of which was unfunded.

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

Methods and Assumptions

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

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

The valuation date was July 1, 2016 and the Projected Unit Credit Cost Method was used. The actuarial assumptions were based on a set of assumptions supplied by the Administration. Turnover rates were based on service and age-related turnover. A discount rate of 3% was used. This rate is the best actuarial estimate of expected long-term experience and is in accordance with guidelines for selection of these rates under GASB 27.

Note 11 - Commitments and contingencies

Commitments

Operating leases and other commitments

The Administration leases certain equipment under various operational lease agreements expiring at various dates through year 2019. In addition, other commitments exist related to contracts for materials and maintenance. Total rental expense under operating leases amounted to approximately $1,584,000 and $1,388,000 for the years ended June 30, 2016 and 2015, respectively.

Note 11 - Commitments and contingencies – (continued)

Commitments – (continued)

Operating leases and other commitments – (continued)

Future minimum rental under the non-cancelable operating leases are as follows:

Year ending June 30,	Amount
2017	$ 2,702,861
2018	1,631,319
2019	766,809
2020	732,209
2021	588,061
Thereafter	23,775
	$ 6,445,034

Government Development Bank Line of Credit

On October 14, 2010, the Legislature of the Commonwealth of Puerto Rico approved a new article 9A to the Law 66 of June 22, 1978, by which it authorized the Administration to incur on obligation up to $285,000,000, under such terms and conditions approved by the Board of Member Institutions (the Board) of the Administration and the Government Development Bank (GDB), as fiscal agent of the Government of Puerto Rico and its instrumentalities.

These additional funds shall be deposited in a special GDB account and may only be used for the following:

a. payment of debts to suppliers, agencies, institutions, reserve fund for the self-insurance (professional responsibility and inter-fund debt) of the Administration; and

b. to provide operational liquidity to ease their fiscal situation, as determined by the agreement with the GDB.

Note 11 - Commitments and contingencies – (continued)

Commitments – (continued)

Government Development Bank Line of Credit – (continued)

From savings generated as a result of the debt renegotiations with the agencies and institutions will create a fund to cover operating expenses related to maintenance, overhaul and reconditioning of the physical plant. The GDB, in its role as fiscal agent, shall possess the administrative mechanisms as it deems necessary to ensure that these funds will be used solely and exclusively for the purposes set forth in Article 9A to law 66 of June 22, 1978. The special bank account created with this subsection and the funds deposited therein shall not be seized, syndicated, frozen, encumbered or otherwise affected by decisions, judgments, orders or rulings issued by courts of Justice of the Government of Puerto Rico or the agencies or public corporations of the Government of Puerto Rico, during any adjudicative proceeding of administrative or judicial nature, regardless of whether they were initiated by private individuals or public institutions.

The Administration was required to develop and implement within one hundred eighty (180) days from the approval of this Article 9A, an aggressive collection plan for the recovery of accounts receivable. The Directors shall report periodically to the GDB on the implementation of that plan, and report annually to the Board and GDB the collection proceeds arising from the execution of the plan. GDB was authorized as fiscal agent to undertake any necessary measures in order to, within a reasonable period of time, help the Administration to become and operate as an independent fiscal instrumentality.

However, once the collection plan is working as expected, and providing the Administration the funds resources required, and became a financially independent institution as determined by GDB, the Administration will be required to assume the remaining established obligations.

The Commonwealth of Puerto Rico will honor the payment of the obligations authorized, with legislative appointments made by the Legislative Body of Puerto Rico on the functional budgets of every fiscal year, beginning with the fiscal year 2012-2013 and ending in the fiscal year 2041-2042.

Note 11 - Commitments and contingencies – (continued)

Commitments – (continued)

Government Development Bank Line of Credit – (continued)

Also, for the fiscal years 2012-2013 and 2013-2014, the Director of the Office of Management and Budget of Puerto Rico (OMB), will consign on the functional budgets of the Commonwealth of Puerto Rico submitted annually by the Governor to the Legislative Body of Puerto Rico, the amount corresponding to interests on the obligations incurred and, beginning on the fiscal year 2014-2015 until fiscal year 2041-2042 the principal and the interest incurred will be consign on the budget. If in any moment the legislative contributions or other income of the Administration weren't enough to cover up the payment of the obligations authorized and the accrued interests, the Secretary of Treasury of Puerto Rico will withdraw from any amounts available in the General Fund of the Commonwealth of Puerto Rico the necessary amounts to repay the principal and interests of the line of credit.

As of June 30, 2016 and 2015, the amount corresponding to the payments of principal and interests for fiscal years 2016 and 2015, were not consign on the budget nor received from the Secretary of the Treasury of Puerto Rico.

Therefore, for 2016 the interest receivable and contribution revenue portion amounting to $16,946,840 was not recognized in the accounting records and for 2015 the interest receivable for $13,144,646 was adjusted to provision for bad debts in the accompanying 2016 statement of revenues, expenses and changes in net position.

Interest expense for the years ended June 30, 2016 and 2015 amounted to $16,946,840 and $16,884,661, respectively. Interest rate on the line of credit is 6%.

The Administration's real property are pledged as collateral to the Government Development Bank loan.

Construction

As of June 30, 2016, the Administration had commitments for approximately $746,000 related to construction contracts.

Note 11 - Commitments and contingencies – (continued)

Contingencies

The Administration is a party in certain legal actions and claims related to medical malpractice arising in the ordinary conduct of its business. Although the Administration appears as a defendant in the claims, many of them involve medical personnel of the member institutions, and in effect, these claims are against said institutions. As a result of the deficiency, as of June 30, 2016 and 2015, of funds available in the Self-Insurance Fund, any unfavorable outcome may have a significant effect on the financial condition of the Administration.

Based on a review of current facts and circumstances management has provided for what is believed to be a reasonable estimate of the exposure to loss associated to litigation. The Administration has established an accrual reserve for claim losses in the amount of $2,300,000 and $2,444,227 at June 30, 2016 and 2015, respectively.

Regulatory issues

The healthcare industry is subject to numerous laws and regulations which include, among other things, matters such as government healthcare participation requirements, various licenses and accreditations, reimbursements for patient services and Medicare and Medicaid fraud and abuse. Government action has increased with respect to investigations and/or allegations concerning possible violations of fraud and abuse and false claims statues and/or regulations by healthcare providers. Providers that are found to have violated these laws and regulations may be subjected to fines or penalties. While management of the Administration believes its policies, procedures and practices comply with governmental regulations, no assurance can be given that the Administration will not be subject to governmental inquires or actions.

Health Insurance Portability and Accountability Act

The Health Insurance Portability and Accountability Act (HIPAA) was enacted in August 1996 to assure health insurance portability, reduce healthcare fraud and abuse, guarantee security and privacy of health information and enforce standards for health information. Organizations are required to be in compliance with HIPAA provisions. Organizations are subject to significant fines and penalties if found not to be compliant with the provisions outlined in the regulations. The Administration's management believes that they are in compliance.

Note 11- Commitments and contingencies – (continued)

Implementation requirements of an Electronic Health Record System

The Health Information Technology for Economic and Clinical Health Act set meaningful use of interoperable Electronic Health Record (EHR) adoption in the health system as a critical national goal and incentivize the EHR adoption. Its goal is not adoption alone but meaningful use of EHRs, that is, their use by providers to achieve significant improvements in care. Meaningful use compliance is required before the Federal Fiscal Year 2016 or otherwise the hospital will incur penalties for non-compliance that may reduce future Medicare payments and potentially Medicare Advantage program payments.

The Centers for Medicare and Medicaid Services (CMS) manages and has implemented an incentive program for those hospitals that implement EHR and that also, comply with certain specific requirements. CMS EHR Incentive Programs provide incentive payments to eligible hospitals as they adopt, implement, upgrade or demonstrate meaningful use, as defined by CMS, of certified EHR technology. As of June 30, 2016, the Administration is under the implementation of its EHR system.

Note 12 - Services to member institutions and medical indigent population

The Administration derives a substantial portion of its revenues from services provided to member institutions. In addition, the Administration provides services to the medical indigent population, which does not have formal means of repayment. Amounts due from member institutions and medical indigent population may be subject to periodic revisions, and/or adjustments based on the availability of funds of the member institutions and/or the Commonwealth of Puerto Rico.

This Space Is Intentionally Left In Blank

Note 13 - Contributions from the Commonwealth of Puerto Rico

Governmental contributions during the years ended June 30, 2016 and 2015, consist of the following:

Description	2016	2015
Funds received in connections with Joint Resolution No. 63 approved by the Commonwealth's Legislature on July 1, 2015, assigned $26.9 million to the Administration for the payment of salaries and operational expenses.	$ 26,886,000	$ -
Funds received in connection with Joint Resolution No. 4533 approved by the Commonwealth's Legislature on August 12, 2004, assigned $40.5 million to the Administration for the construction of new Trauma facilities, the establishment of a Gamma Knife Center, a blood bank, improvement to the emergency room and purchase of equipment.	-	7,370
Funds received in connection with Law No. 242 approved by the Commonwealth's Legislature on December 13, 2011, assigned $3.4 million to the Administration for the acquisition of medical equipment.	-	236,303
Funds received in connection with Joint Resolution No. 22 approved by the Commonwealth's Legislature on June 30, 2013, assigned $3.5 million to the Administration for the acquisition of medical equipment.	-	1,197,905
Funds received in connection with Joint Resolution No. 46 approved by the Commonwealth's Legislature on July 1, 2014, assigned $27.9 million for the payment of payroll and for the Emergency and Trauma facilities in Río Piedras.	-	27,791,499

Note 13 - Contributions from the Commonwealth of Puerto Rico – (continued)

Funds receivable in connection with Law 66 approved by the Commonwealth's Legislature on June 22, 1978, for the payment of principal and interest on the GDB line of credit.	-	16,884,661
Funds received in connection with a request to the Office of Management and Budget of Puerto Rico for the acquisition of medical equipment.	401,780	-
Funds received in connection with Joint Resolution of Special Assignment No. 17-2013 approved by the Commonwealth's Legislature on January 31, 2013, for the contribution to the Retirement System.	479,833	479,199
Donations	2,000	12,525
	$ 27,769,613	$ 46,609,462

Note 14 - Going concern and management plans

As of June 30, 2016 and 2015, the Administration has a total deficit of $873,242,319 and $739,377,466, respectively, and a deficiency in working capital of $144,352,638 and $101,479,907, respectively. These conditions raise substantial doubts about the Administration's ability to continue as a going concern. The financial condition of the Administration has weakened by high operating costs and recurring operating losses, which have affected its ability to pay its suppliers, governmental agencies and other creditors on a regular basis. In addition, the Administration has been affected by the delay in collection of billings for services rendered to member institutions due to the lack of cash flow among said institutions. The Administration's operations will depend on obtaining additional contributions from the Secretary of the Puerto Rico Department of Health and the Commonwealth of Puerto Rico to partially subsidize existing and future operating losses, resulting from high operating costs and services provided to the medical indigent population not covered under any private health insurance or non-participating in the Health Reform Program Administered by the Puerto Rico Health Insurance Administration (ASES). The Administration's operations will depend on the following critical factors to partially subsidize existing and future operating losses:

Note 14 - Going concern and management plans – (continued)

1. Implementation Law 66 (Fiscal Sustainability) – Effective June 17, 2014, rule 66 was deployed in the Administration. As a result, operational costs will decrease by $34 million in the following three 3 fiscal years. This includes re-negotiation and new agreements reached with the union organization (UGT-"Union General de Trabajadores).

2. Transformation in financial Model –ACAA – Effective July 1, 2014, a new financial model was agreed, signed off and implemented by the Administration and ACAA (Administración de Compensaciones por Accidentes Automovilísticos). Under this agreement, ACAA agreed to pay off existing accumulated balance of $6 million, $4 million were paid upfront in July 2014, and subsequent payments reconciled bills up to $2 million. By June 30, 2015, $1.3 million were collected of this amount. In addition, the agreement includes a contracting structure change from a "fee for service" universal platform to a monthly lump sum capitation payment of $700,000. This is a 40% payment increase compared to contracts in place during previous years. From the management standpoint, the agreement includes ACCA-Administration monthly meeting geared towards the ongoing evaluation of medical costs incurred for ACCA patients, actuarial insights regarding submitted claims, and better operational results regarding the efficiency of the claims management process incurred by both parties. This agreement expires on June 30, 2017 and we will be working on getting an increase in the monthly capitation payment to bring this amount to at least $1 million monthly.

3. During 2016, we continued with the initiative begun in January 2015, which includes redefinition of actual Private and Government Insurer Contracts and Rates, which includes the following strategies regarding existing insurance contracts:
   a. ***Revision and analysis of contracted versus actual services provided and distributed by Emergency Room, Ancillary, Respiratory, Hospital, and Outpatient medical services*** - Non-contracted services will be included in existing contracts with corresponding negotiated rates.
   b. ***Re-distribution of contracted bundled services*** – Existing bundled services and rates will be revised. Services which prove to be more costly will be re-negotiated and billed separately with corresponding rates.
   c. ***Revision of overall rate structure and billing model*** – Rates of existing contracts will be re-negotiated based on the cost of providing medical services, frequency and severity of claims, types of services provided (tertiary and supra-tertiary), and the risk assumed by the Administration, which is dictated by its public policy.

Note 14 - Going concern and management plans – (continued)

4. A**ggressive collection efforts regarding Private and Government Insurance Receivables-** During 2016, we continued with the initiative begun in January 2015, which includes, an aggressive collections management plan including Rule 65-2013 has been deployed by the Administration personnel. This plan includes but is not limited to:
    a. Ongoing account receivable key performance measurements and aging by insurer
    b. Ongoing account receivable key performance measurements and aging for non-insured patients
    c. Follow up collections system for segments a. and b.

5. In April 2015, the Commonwealth of Puerto Rico changed the existing model of the government's health plan known as "Mi Salud", now they are 5 health insurance plans. During 2016, we developed the following strategies to ensure that the cash flow was not affected:
    a. With the insurers of greater economic impact they were asked for a monthly advance payment that would be amortized with the monthly billing.
    b. Get a correct assembly of the electronic invoicing so that the invoices are not returned.

6. A**ggressive collection efforts regarding Administration Consumer Institution Receivables –** During 2016, we continued with the initiative begun in January 2015, which includes and aggressive collections management plan has been deployed for this segment of the Administration, which represents approximately 68% of its total receivable. This plan includes but is not limited to:
    a. Request non-government consumer institutions, at the beginning of each fiscal year, to provide the Administration with certified financial statements including a certification of payment for services to be provided.
    b. Regarding participating institutions, the Director of the OMB (Office of Management and Budget) will be notified of existing debts. According to the Administration's Rule 66, the OMB office can transfer these quantities directly.
    c. Request the Treasury Secretary to send the Administration payments directly on behalf of government consumer institutions which are in debt.

7. Efforts to improve the accuracy and timeliness of billing and recover our cost:
    a. Consumer Institutions
        i. Effective July 1, 2015, the prices for services provided were increased by 5%, together with efforts to provide new services or regain lost customers of this type, we can maintain the amount required in institutional revenues.

Note 14 - Going concern and management plans – (continued)

ii. Another effort will be aimed at keeping the billing 30 days and reconciliation of the pending bill 90 days.
iii. It is periodically reconciled with the consumer institutions and claims dealt with promptly to reduce bad debt expense.

b. Health Plan- Within this initiative, the Administration decided to move closer billers to service areas. Currently have four large areas where invoice: Emergency Room, Radiology and Laboratory Services, Inpatient and External Clinics and Headquarters.

   i. We'll get more accurate patients register, which will reduce in $3.5 million the number of patients without health plan in two years.
   ii. Better coordination between billers, medical records, patient registration and utilization, what will bring an increase in revenues.
   iii. On average will reduce to 30 days the time to bill what will make the recovery and detection of errors faster.

8. Deployment of a new management Platform: "Hacia la Reconceptualización del Centro Médico de Puerto Rico" **-** focused on the following strategic initiatives:

   a. Systemic Thinking
   b. Integrated Management based on the identification of core business processes, measurements, corrective and preventive actions
   c. Continuous Education
   d. Internal and External Communication

9. Transformation of the Administration's Structure:
   a. Governor Executive Orders OE-2013-0150 and 2014- 011, which order requirements to comply with the integration and consolidation of ASEM and the University District Hospital (UDH). This order highlights the following recommendations:

      i. To obtain more relevant information of all the Medical Center Components, in addition to the information included in the report, to determine necessary changes and to establish the feasibility criteria for a transformation of the Medical Center.

10. Get a greater contribution from the Commonwealth of Puerto Rico to try to recover operational costs and the deficiency in contractual adjustment.

Note 14 - Going concern and management plans – (continued)

11. Strategies were developed to control the Administration's operational expenditure that would include the following:
    a. In the costs of wages and marginal benefits will freeze positions that are not from direct care to patient and reduction in overtime.
    b. Control purchases of materials and medicines and requesting bids for the purchase of implants, which will bring an economy of around $2 million annually.
    c. Plan to reduce the utilities expense and elimination and / or reduction of non-medical professional services contracts which will bring an economy of around $1.5 million annually.

The ability of the Administration to continue as a going concern is dependent on the success of management's plans. The financial statements do not include any adjustments that might be necessary if the Administration is unable to continue as a going concern.

Note 15 - Concentration of credit – patients' accounts receivable

The Administration grants credit without collateral to its patients, most of whom are residents of Puerto Rico and are insured under third-party payor agreements.

The mix of receivables from patients and third-party payors at June 30, 2016 and 2015, is as follows:

	2016	2015
ACAA	2%	3%
Humana Insurance	7%	7%
Triple S	9%	13%
Self payors	47%	45%
Other Insurances	26%	20%
MCS	4%	6%
Medicare	4%	4%
Correctional Health Sevices	1%	2%
	100%	100%

Note 16- Functional expenses

The Administration provides general health care services. Expenses, related to providing these services for the years ended June 30, 2016 and 2015, are as follow:

	2016	2015
Health care services	$ 161,435,831	$ 158,722,178
General and administrative and depreciation	109,280,031	46,488,080
	$ 270,715,862	$ 205,210,258

Note 17 - Restatement

During May 2018, the Employee Retirement System (ERS) of the Commonwealth of Puerto Rico provided the information needed to adopt the Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions,* an amendment of GASB Statement No. 27, and GASB Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date,* an amendment of GASB Statement No. 68. Accordingly, and as fully disclosed in Note 9, the financial statements as of and for the year ended June 30, 2015 have been restated to report the results of the adoption of these pronouncements.

The effect of these restatement adjustments on the Administration's net position as of July 1, 2014 is as follows:

Net position (deficit) as previously reported	$ (302,325,876)
Restatement adjustments:	
Impact of GASB No. 68 implementation - net pension liability	(405,448,870)
Impact of GASB No. 68 implementation - employer contribution	10,150,846
	(395,298,024)
Net position (deficit), as restated	$ (697,623,900)

This Space Was Intentionally Left In Blank

Note 17 - Restatement – (continued)

The effect of these restatement adjustments on the Administration's financial statements as of June 30, 2016 and 2015 are as follows:

June 30, 2016	As originally reported	As adjusted	Effect of change
Statement of Net Position (Deficit)			
Deferred outflows of resources - pension related	-	121,732,252	121,732,252
Net pension liability	-	(609,076,916)	(609,076,916)
Deferred inflows of resources - pension related	-	(10,565,214)	(10,565,214)
Statement of Revenues, Expenses, and Changes in Net Position (Deficit)			
Pension expense	-	76,413,531	76,413,531
Statement of Cash Flows			
Deferred outflows of resources - pension related	-	(35,870,434)	(35,870,434)
Net pension liability	-	104,904,256	104,904,256
Deferred inflows of resources - pension related	-	7,379,709	7,379,709

June 30, 2015	As originally reported	As adjusted	Effect of change
Statement of Net Position (Deficit)			
Deferred outflows of resources - pension related	-	85,861,818	85,861,818
Net pension liability	-	(504,172,660)	(504,172,660)
Deferred inflows of resources - pension related	-	(3,185,505)	(3,185,505)
Statement of Revenues, Expenses, and Changes in Net Position (Deficit)			
Pension expense	-	26,198,423	26,198,423
Statement of Cash Flows			
Deferred outflows of resources - pension related	-	(85,861,818)	(85,861,818)
Net pension liability	-	108,874,636	108,874,636
Deferred inflows of resources - pension related	-	3,185,505	3,185,505

Note 18 - <u>Subsequent events</u>

The Administration evaluated subsequent events through August 9, 2017 (except as to Notes 9, 17 and 18, which are as of November 15, 2018), which is the date the financial statements were available to be issued. Except as described below, no events have occurred subsequent to the statement of net position date that would require additional adjustment to, or disclosure in the financial statements.

On September 20, 2017, Hurricane María impacted Puerto Rico causing widespread infrastructure and other property damage, however, no significant property losses were experienced by the Administration.

On June 27, 2017, the Treasury Department issued Circular Letter No. 1300 4617 in order to convey to the Primary Government's agencies, public corporations and municipalities the new implementation procedures to adopt, effective, July 1, 2017, the new "pay as you go (PayGo}" mechanism for all of the Commonwealth's Retirement Systems. With the start of the fiscal year 2018, employers' contributions, contributions ordered by special laws and the Additional Uniform Contribution were all eliminated and replaced by a monthly PayGo charge that will be collected from the aforementioned government entities to pay retirees. The Commonwealth Retirement Systems will determine and administer the payment amount per retiree that will be charged to each agency, public corporation and municipality. The PayGo charge must be submitted to the Treasury Department before the 15th day of each month along with the individual contributions withheld from active employees. As liquid retirement funds become depleted, the PayGo charge is expected to increase.