COMMONWEALTH OF PUERTO RICO

SOCIOECONOMIC AND COMMUNITY DEVELOPMENT OFFICE

FINANCIAL STATEMENT – CASH BASIS, REQUIRED SUPPLEMENTARY INFORMATION AND INDEPENDENT AUDITORS' REPORT (WITH THE ADDITIONAL REPORTS AND INFORMATION REQUIRED BY THE *GOVERNMENT AUDITING STANDARDS* AND THE *UNIFORM GUIDANCE*)

For the Fiscal Year Ended June 30, 2018

1208 Ave. Franklin D Roosevelt

San Juan Puerto Rico 00920

Visit our website at www.odsec.pr.gov/

Jesús Vélez Vargas, Executive Director

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López-Vega, CPA, PSC
Certified Public Accountants / Management Advisors

INDEPENDENT AUDITORS' REPORT

To the Executive Director
Commonwealth of Puerto Rico
Socioeconomic and Community Development Office
San Juan, Puerto Rico

Report on the Financial Statements

We have audited the accompanying cash basis financial statement of the **Socioeconomic and Community Development Office (Office),** which comprise statement of cash receipts and disbursement – governmental funds for the fiscal year ended June 30, 2018, and the related notes to the financial statement.

Management's Responsibility for the Financial Statement

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, 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 statement 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 statement.

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

Calle Paraná #1686, El Cerezal, San Juan, P.R. 00926-3144 – Tel. (787) 777-8044 / Fax (787) 764-9377

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Summary of Opinions

Opinion Unit	Type of Opinion
General Fund	Unmodified
Community Services Block Grant – Federal	Unmodified
Community Development Block Grant – Federal	Unmodified
Others Funds	Unmodified

Opinion

In our opinion, the financial statement referred to above present fairly, in all material respects, the cash receipts and disbursements of the **Office** for the year ended June 30, 2018, in conformity with the basis of accounting described in **Note 1**.

Emphasis of Matters

Uncertainty about Ability to Continue as a Going Concern – Primary Government

The accompanying financial statements of the **Office** have been prepared assuming that the Commonwealth will continue as a going concern. As discussed in **Note 7** to the financial statements, the Commonwealth's recurring deficits, negative financial position, further deterioration of its economic condition, and inability to access the credit markets raises substantial doubt about the Commonwealth's ability to continue as a going concern. Management's plans regarding these matters are also described in **Note 7**. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinions are not modified with respect to this matter.

Basis of Accounting

As described in **Note 1**, the **Office** prepares its financial statement on the basis of cash receipts and cash disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

Also, as described in **Note 1**, the financial statement of the **Office** are intended to present the cash receipts and cash disbursements of only that portion of the financial reporting entity of the Commonwealth of Puerto Rico that is attributable to the transactions of the **Office**.

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages **5** through **9** and **29** be presented to supplement the financial statement. Such information, although not a part of the financial statement, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context.

We have applied certain limited procedures to the required supplementary information in accordance with the auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statement, and other knowledge we obtained during our audit of the financial statement. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the **Office's** basic financial statements. The accompanying schedule of expenditures of federal awards, as required by *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Costs Principles, and Audit Requirements for Federal Awards Uniform Guidance*, on pages **31** and **32**, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements.

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

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2019, on our consideration of **Office's** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering **Office's** internal control over financial reporting and compliance.

López-Vega, CPA, PSC

LOPEZ–VEGA, CPA, PSC

San Juan, Puerto Rico
October 31, 2019
Stamp No. 2758860 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

INTRODUCTION

As management of the **Socioeconomic and Community Development Office (Office)**, we offer to the readers of this annual financial report our discussion and analysis of the **Office's** financial performance during the fiscal year ended June 30, 2018. The following discussion and analysis has been designed to accomplish the following goals:

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

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

ORGANIZATION AND MISSION STATEMENT

Law 10-2017

Law 10-2017, creates the **"Socioeconomic and Community Development Office" (known as ODSEC by its Spanish acronym).** Under the provisions of this Act the **Office of the Commissioner for Municipal Affairs (OCAM)** transferred to **Office** the administration of federal funds known as "Community Development Block Grant"(CDBG), the special funds includes Community Development Block Grant Fund, CDBG - Disaster Recovery Enhancement Fund, CDBG - Neighborhood Stabilization Fund and Section 108 Loan Program, known as the "Loan Guarantee Assistance Under Section 108".

In addition, the **Office** receive and administer the "Community Services Block Grant"(CSBG) to provide assistance to a network of community-based organizations for programs and services to ameliorate the causes and consequences of poverty and to revitalize low-income communities. Also, the **Office** and receive and administer the "Juvenile Justice and Delinquency Prevention Fund" to supports states and communities in their efforts to development and implement effective and coordinated prevention and intervention programs and to improve the juvenile justice system so that protects public safety, holds justice-involved youth appropriately accountable, and provides treatment and rehabilitative services tailored to the needs of juveniles and their families.

The **Office** is responsible for carrying out the programs of the Commonwealth directed toward the development of the low-income communities in Puerto Rico. In addition, the **Office** acts as a coordinator social service programs or programs of any related nature giving emphasis to the self-motivation of individuals to achieve good life conditions and develop their skills to reach an economic and social independence.

Through its own actions or in coordination with other government or private organizations, the **Office** carries out programs of direct training to low income persons, motivation and training programs, community improvement projects, programs to organize the communities' leaders, guidance programs for individuals and families and any other activity which leads to the social improvement of communities as wells as of individuals.

The operations of the **Office** are funded through annual budgetary appropriations approved by the Legislature of the Commonwealth of Puerto Rico. The annual budgetary appropriation amounted to $2,893,000, for the fiscal year ended June 30, 2018. In addition, the **Office** receives state funds assignment by Commonwealth Legislature Resolutions. During the fiscal year ended June 30, 2018 the **Office** received $2,705,500 from Legislature Resolutions.

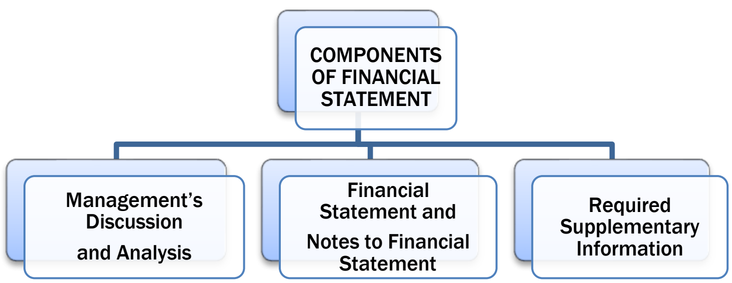
FINANCIAL HIGHLIGHTS

- In the **Office** Statement of Cash Receipts and Cash Disbursements – Governmental Fund Types, the actual cash receipts exceeded actual cash disbursements by $12,199,285.
- The General Fund (the primary operating fund) cash receipts amounted to $2,893,000 and represents 5.60% of total cash receipts during the fiscal year.
- The General Fund (the primary operating fund) cash disbursements amounted to $2,012,620 and represents 5.10% of total cash disbursement for the fiscal year.
- During the fiscal year 2018, federal funds received amounted to $45,662,983 and federal funds disbursements amounted to $36,911,078.
- On a budgetary basis, actual cash receipts exceeded actual cash disbursements by $880,380.

FINANCIAL STATEMENT PRESENTATION

Overview of the Financial Statement

The **Office's** financial statement comprises three components: (1) management discussion and analysis, (2) basic financial statement, and (3) required supplementary information.



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

  The Statement of Cash Receipts and Cash Disbursements presents, within its cash receipts, the funds appropriated by the Commonwealth and the grants received from U.S. Department of the Interior. It also presents its cash disbursements by program. The difference between the cash receipts and cash disbursements is presented as an excess or deficiency for the year. All this combined provides the general financial information of the **Office**; however, other nonfinancial factors shall be considered within any comprehensive analysis.

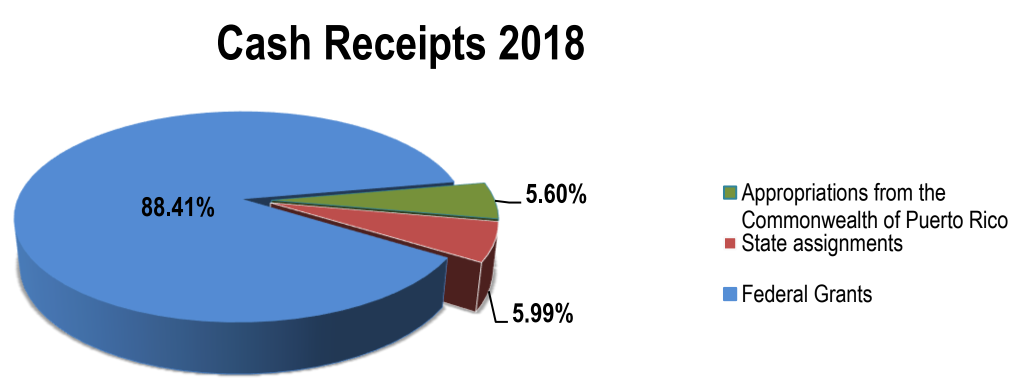
- **Notes to the Financial Statement** – Provides integral information needed to explain the basis for the numbers used within the Financial Statement and provide more detailed data.
- **Required Supplementary information** – Provides additional information to better understand the financial position of the **Office** and contains the Budgetary Comparison Schedule for the General Fund.

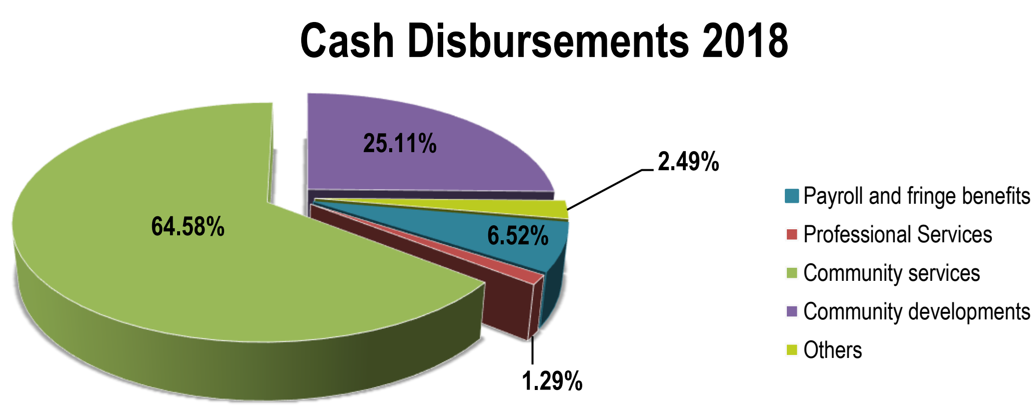
➢ FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE

Governmental Fund Financial Statement

The governmental fund financial statements focus on major funds. The **Office's** major funds are the general fund (which accounts for the main operating activities of the **Office**) and federal fund (which account for all grants received from the federal programs). The **Office's** Statement of Cash Receipts and Cash Disbursements for fiscal year ended June 30, 2018, presented those four major funds: 1) General Fund; 2) Community Service Block Grant; 3) Community Development Grant; and 4) Other Funds.

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





FINANCIAL ANALYSIS OF THE AGENCY AS A WHOLE (CONTINUED)

GENERAL FUND BUDGETARY HIGHLIGHTS

A budget is prepared for the General Fund and represents legislative appropriations for the general operation of the **Office**. The procedures followed for approval and operations of the budget are defined by the laws of Commonwealth of Puerto Rico. On a budgetary basis, actual cash receipts exceeded actual cash disbursements by $880,380.

ECONOMIC FACTORS

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

As more fully explained in **Notes 7, 8** and **9** to the financial statement, the Governments of the United States of America and the Commonwealth of Puerto Rico have approved and implemented certain laws to overcome this crisis. Following are some of the measurements implemented to this end:

- ***Effect of Commonwealth***

  The Commonwealth is currently facing a profound fiscal and economic crisis. As a result of this situation, and pursuant to PROMESA, the Oversight Board designated the Commonwealth as a covered entity. Furthermore, on May 3, 2017, a petition of relief was filed by the Oversight Board under Title III of PROMESA, incorporating the automatic stay provisions of Bankruptcy Code section 362 and 922. As a covered entity, the Commonwealth was required to prepare and eventually revise its Fiscal Plan.

- ***Hurricanes Irma (DR-4336) and María (DR-4339)***

  During the month of September 2017, Puerto Rico suffered the passing of Hurricane Irma and María, causing catastrophic damages to the infrastructure and the collapsing of the electric power grid and the telecommunications system of the entire Island. The Island was declared a major disaster area by the President of the United States on September 20, 2017 and approximately $508 million dollars in public assistance grants have been obligated. Many citizens lost their homes and the business sector suffered heavy losses due to infrastructure damages, looting during and after the hurricanes, loss of inventory and the absence of electric power, which forced businesses to invest in power generators to operate, incurring in significant gasoline and diesel expenses.

  The Commonwealth of Puerto Rico and the Financial Oversight and Management Board are working with the Federal Emergency Management Agency (FEMA) on the recovery of the Island, but the recuperation efforts have taken several months in other to bring back a certain level of normalcy to the everyday life of Puerto Rico's citizens. The U.S. President and Congress have been working on the assignment of federal assistance of approximately $94 million, mainly for the reconstruction of the electric infrastructure and housing assistance for the residents of Puerto Rico.

FINANCIAL CONTACT

The **Office**'s financial statements are designed to present the readers with a general overview of the cash receipts and cash disbursements of the **Office**. Questions or concerns regarding any information in this report or requests for additional information should be addressed to the Commonwealth of Puerto Rico **Socioeconomic and Community Development Office** Executive Director, 1208 Ave. Franklin D Roosevelt, San Juan Puerto Rico 00920.

Statement of Cash Receipts and Cash Disbursements – Governmental Funds
For the Fiscal Year Ended June 30, 2018

	General Fund	Community Services Block Grant – Federal	Community Development Block Grant – Federal	Other Funds	Total Governmental Funds
CASH RECEIPTS					
Appropriations from the Commonwealth of Puerto Rico	$ 2,893,000	$ -	$ -	$ -	$ 2,893,000
State assignments	-	-	-	3,092,036	3,092,036
Federal Grants	-	22,182,793	23,078,405	401,785	45,662,983
Total receipts	2,893,000	22,182,793	23,078,405	3,493,821	51,648,019
CASH DISBURSEMENTS					
Payroll and fringe benefits	1,634,578	134,822	762,622	41,425	2,573,447
Professional services	144,950	283,483	73,125	9,300	510,858
Equipments	4,000	1,490	-	-	5,490
Supplies and materials	14,560	11,358	8,274	-	34,192
Permanent improvements	97,356	-	-	-	97,356
Utilities	82,140	104,900	-	-	187,040
Transportation	26,163	10,368	2,156	-	38,687
Community services	-	25,474,876	-	-	25,474,876
Community developments	-	-	9,906,094	-	9,906,094
Others	8,873	86,785	-	525,036	620,694
Total disbursements	2,012,620	26,108,082	10,752,271	575,761	39,448,734
Excess of cash receipts over (under) cash disbursements	$ 880,380	$ (3,925,289)	$ 12,326,134	$ 2,918,060	$ 12,199,285

See accompanying notes to financial statement – cash basis

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Law 10-2017, creates the **"Socioeconomic and Community Development Office" (known as ODSEC by its Spanish acronym).** Under the provisions of this Act the **Office of the Commissioner for Municipal Affairs (OCAM)** transferred to **Office** the administration of federal funds known as "Community Development Block Grant"(CDBG), the special funds includes Community Development Block Grant Fund, CDBG - Disaster Recovery Enhancement Fund, CDBG - Neighborhood Stabilization Fund and Section 108 Loan Program, known as the "Loan Guarantee Assistance Under Section 108".

In addition, the **Office** receive and administer the "Community Services Block Grant"(CSBG) to provide assistance to a network of community-based organizations for programs and services to ameliorate the causes and consequences of poverty and to revitalize low-income communities. Also, the **Office** receive and administer the "Juvenile Justice and Delinquency Prevention Fund" to supports states and communities in their efforts to development and implement effective and coordinated prevention and intervention programs and to improve the juvenile justice system so that protects public safety, holds justice-involved youth appropriately accountable, and provides treatment and rehabilitative services tailored to the needs of juveniles and their families.

The **Office** is responsible for carrying out the programs of the Commonwealth directed toward the development of the low-income communities in Puerto Rico. In addition, the **Office** acts as a coordinator social service programs or programs of any related nature giving emphasis to the self-motivation of individuals to achieve good life conditions and develop their skills to reach an economic and social independence.

Through its own actions or in coordination with other government or private organizations, the **Office** carries out programs of direct training to low income persons, motivation and training programs, community improvement projects, programs to organize the communities' leaders, guidance programs for individuals and families and any other activity which leads to the social improvement of communities as wells as of individuals.

The operations of the **Office** are funded through annual budgetary appropriations approved by the Legislature of the Commonwealth of Puerto Rico. The annual budgetary appropriation amounted to $2,893,000, for the fiscal year ended June 30, 2018. In addition, the **Office** receives state funds assignment by Commonwealth Legislature Resolutions. During the fiscal year ended June 30, 2018 the **Office** received $2,705,500 from Legislature Resolutions.

The main programs administered by the **Office** consist of:

1. **Community Services Block Grant** – The objective of this program is to provide assistance to a network of community-based organizations for programs and services to ameliorate the causes and consequences of poverty and to revitalize low-income communities. Funds can be used to fund programs and other activities that assist low-income individuals and families attain self-sufficiency; provide emergency assistance; support positive youth development; promote civic engagement; and improve the organization infrastructure for planning and coordination among multiple resources that address poverty conditions in the community.

2. **Community Development Block Grant** – The primary objective of this program is to provide assistance to the development of viable communities by providing decent housing, a suitable living environment, and expanded economic opportunities, principally for persons of low- and moderate-income. This objective can be achieved in two ways. First, funds can only be used to assist eligible activities that fulfill one or more of three national objectives. Second, the grantee must spend at least 70 percent of its funds over a period of up to 3 years, as specified by the grantee in its certification, for activities that address the national objective of benefiting low- and moderate-income persons.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization (continued)

3. **Juvenile Justice and Delinquency Prevention Fund** – This fund is used to account for the proceeds for the resources received from the United States Department of Justice. This program supports states and communities in their efforts to develop and implement effective and coordinated prevention and intervention programs and to improve the juvenile justice system so that it protects public safety, holds justice-involved youth appropriately accountable, and provides treatment and rehabilitative services tailored to the needs of juveniles and their families.

Financial Reporting Entity

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

The financial information included in the accompanying Statement of Cash Receipts and Cash Disbursements was obtained from the Puerto Rico Treasury Department's Integrated Financial Accounting System (PRIFAS) and is issued solely to comply with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States of America and for the information to the federal awarding agencies, pass-through entities, regulators, management and those charged with the governance.

Measurement Focus and Basis of Accounting

The **Office's** accompanying financial statement has been prepared in accordance with the cash basis of accounting, which is a special purpose framework other than generally accepted accounting principles (GAAP) in the United States of America, as established by the Governmental Accounting Standards Board (GASB).

The basis of accounting involves the reporting of only cash and cash equivalents and the changes therein resulting from cash inflows (cash receipts) and cash outflows (cash disbursements) reported in the period in which they occurred. This cash basis of accounting differs from GAAP primarily because revenue is recognized when received in cash rather than when earned and subject to accrual, and expenditures are recognized when paid rather than when incurred to subject to accrual.

This financial statement has been prepared pursuant to the provision of Law No. 230 of July 23, 1974, as amended, known as the "Puerto Rico Government Accounting Act". This law establishes public policy with respect to the control of an accounting for public funds and property. The **Office** funds are, by law, under custody and control of the Secretary of Treasury in the PRIFAS accounting system.

Financial information of the **Office** is presented in this report as follow:

1. Management's discussion and analysis – Introduces the basic financial statements and provides an analytical overview of the **Office** financial activities.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Measurement Focus and Basis of Accounting (continued)

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

   The Statement of Cash Receipts and Cash Disbursements presents, within its cash receipts, the funds appropriated by the Commonwealth and the grants received from U.S. Department of the Interior. It also presents its cash disbursements by program. The difference between the cash receipts and cash disbursements is presented as an excess or deficiency for the year. All this combined provides the general financial information of the **Office**; however, other nonfinancial factors shall be considered within any comprehensive analysis.

3. Notes to the Financial Statements – Provides integral information needed to explain the basis for the numbers used within the Financial Statement and provide more detailed data.

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

Governmental fund types

Governmental funds are those through which most governmental functions are financed. The acquisition uses and balances of the **Office** expendable financial resources and the related current liabilities are accounted for through governmental funds. The measurement focus is upon determination of changes in financial position, rather than upon net income determination. Fund financial statements focus on information about the **Office** major governmental funds. Major individual governmental funds are reported as separately columns in the Statement of Cash Receipts and Cash Disbursements on the cash basis of accounting.

The following are the **Office** major governmental fund types:

1. **General Fund** – is the general operating fund of the **Office**. It is used to account for and report all financial resources, except for those required to be accounted for in another fund. It is presumed that the **Office's** governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) USGAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than general fund. Its revenue consist mainly of state appropriations.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Governmental fund types (continued)

2. **Community Services Block Grant – Federal** – This is fund used to account for and report the proceeds of revenues derived from Commonwealth of Puerto Rico Administration for Children and Families, used to provide assistance to a network of community-based organizations for programs and services to ameliorate the causes and consequences of poverty and to revitalize low-income communities. Funds can be used to fund programs and other activities that assist low-income individuals and families attain self-sufficiency; provide emergency assistance; support positive youth development; promote civic engagement; and improve the organization infrastructure for planning and coordination among multiple resources that address poverty conditions in the community.

3. **Community Development Block Grant – Federal** – This is fund used to account for the CDBG resources received from the United States Department of housing and Urban Development (HUD) related to community development, that are legally restricted to expenditures for specified purposes.

4. **Others Funds** – Is a governmental fund used to account for and report the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted or committed to expenditure for specified purposes other than debt service or capital projects. Resources restricted or committed to expenditure for purposes normally financed from the general fund are generally accounted for in the general fund provided that all applicable legal requirements can be appropriately satisfied, and the use of special revenue funds is not required unless they are legally mandated.

Property and equipment acquisition

Property and equipment resulting from cash transactions are reported as cash disbursements in the acquiring governmental fund upon cash acquisition. No capital assets are recorded in Office's financial statement. No long-term debt is reported in **Office's** financial statement.

Inventory purchases

The **Office** purchases office and printing supplies, gasoline, oil and other items. The cost of purchases is recorded as a cash disbursement and, consequently, the inventory is not recorded in the financial statements.

Interfund transactions

The **Office** has the following types of transactions among funds:

1. **Interfund transfers**

   Interfund transfers represent temporary loans between the funds.

2. **Operating transfers**

   Operating transfers represent transfers between funds to specific purposes designated by the management.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated absences

The **Office** employees' are granted 15 days of vacation and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of 60 days and sick leave up to a maximum of 90 days. In the event of an employee resignation, the employee is reimbursed for accumulated vacation days up to the maximum allowed. Separation from employment prior to the use of all or part of the sick leave before 10 years of service terminates all rights for compensation. Employee's vested annual leave is recorded as expenditure when utilized. No accrued compensated absences are reported in **Office's** financial statement. Compensated absences resulting from cash transactions are reported as cash disbursements in the governmental funds column upon cash payment.

Insurance

The **Office** has insurance coverage for its public facilities, primarily to provide protection from catastrophic losses. The Secretary of the Treasury Department of the Commonwealth of Puerto Rico is the agent commissioned to place all of the **Office**'s insurance coverage.

Claims and judgments

The amount owed by the **Office** for claims and judgments, if any, which is due on demand, such as from adjudicated or settled claims, are recorded when paid.

Accounting for pension costs

Effective on July 1, 2017, the Office and other participants of the ERS converted to a new "PayGo" model. Under the "PayGo" funding, the participant employers directly pay the pension benefits as they are due rather than attempt to build up assets to pre-fund future benefits. "PayGo" payments are recorded as expenditures\expenses in the financial statements.

At that date, the Office's pension costs accounting transitioned from GASB Statement No. 68 to the requirements of GASB Statement No. 73 "Accounting and Financial Reporting For Pensions and Related Assets That Are Not Within The Scope of GASB No. 68". Accordingly, pension costs are reported based on the employer total pension liability, pension expense and deferred outflows/inflows of resources reported by the ERS. For purposes of measuring, pension costs have all been determined on the same basis as they are reported by the ERS.

Accounting for other postemployment benefits ("OPBED")

GASB Statement No. 75 "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions" is effective for the Agency starting on July 1, 2017. As required by the accounting pronouncement, OPEB transactions should be accounted based on its proportional share of the collective net OPEB liability, OPEB expense and deferred outflows/inflows of resources reported by the Plan. For purposes of measuring, OPEB costs should have all been determined on the same basis as they are reported by the Plan. The ERS has not issued its 2017 basic financial statements, nor has it provided to the Agency with the required information to implement the referred accounting pronouncement. The Agency's contribution for OPEB is included as part of the "PayGo" charges billed on a monthly basis by the Puerto Rico Department of Treasury ("PRDT"). "PayGo" payments are recorded as expenditures\expenses in the financial statements.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Adoption of new accounting pronouncements

Effective July 1, 2017, the **Office** adopted the provisions of the following GASB Statements:

1. **GASB Statement No. 75 *"Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions."*** The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement replaces the requirements of Statements No. 45, "*Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions"*, as amended, and No. 57, "*OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*". The provisions of this Statement are effective for fiscal years beginning after June 15, 2017 (fiscal year ended June 30, 2018).

2. ***GASB Statement No. 81 "Irrevocable Split-Interest Agreements".*** The objective of this Statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. This Statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement. Furthermore, this Statement requires that a government recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party, if the government controls the present service capacity of the beneficial interests. This Statement requires that a government recognize revenue when the resources become applicable to the reporting period. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2016 (fiscal year ended June 30, 2018), and should be applied retroactively.

3. **GASB Statement No. 85 "Omnibus 2017".** The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). The requirements of this Statement are effective for reporting periods beginning after June 15, 2017 (June 30, 2019).

4. **GASB Statement No. 86 "Certain Debt Extinguishment Issues".** The primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. The requirements of this Statement are effective for reporting periods beginning after June 15, 2017 (June 30, 2019).

   The implementation of these Statements has no significant impact on the **Office's** financial statements – cash basis for the fiscal year ended June 30, 2018.

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Future adoption of accounting pronouncements

The GASB has issued the following statements, which the Office has not yet adopted:

1. **GASB Statement No. 83 *"Certain Asset Retirement Obligations".*** This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this Statement. This Statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for AROs.

   This Statement requires that recognition occur when the liability is both incurred and reasonably estimable. The determination of when the liability is incurred should be based on the occurrence of external laws, regulations, contracts, or court judgments, together with the occurrence of an internal event that obligates a government to perform asset retirement activities.

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

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

   This Statement also requires disclosure of information about the nature of a government's AROs, the methods and assumptions used for the estimates of the liabilities, and the estimated remaining useful life of the associated tangible capital assets. If an ARO (or portions thereof) has been incurred by a government but is not yet recognized because it is not reasonably estimable, the government is required to disclose that fact and the reasons therefor. This Statement requires similar disclosures for a government's minority shares of AROs. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018 (fiscal year ended June 30, 2019).

2. **GASB Statement No. 84 *"Fiduciary Activities".*** The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018 (June 30, 2020).

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Future adoption of accounting pronouncements (continued)

3. **GASB Statement No. 85 *"Omnibus 2017".*** The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). The requirements of this Statement are effective for reporting periods beginning after June 15, 2017 (June 30, 2019).

4. **GASB Statement No. 86 *"Certain Debt Extinguishment Issues".*** The primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. This Statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to financial statements for debt that is defeased in substance. The requirements of this Statement are effective for reporting periods beginning after June 15, 2017 (June 30, 2019).

5. **GASB Statement No. 87 *"Leases".*** The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2019 (June 30, 2021). Earlier application is encouraged. Leases should be recognized and measured using the facts and circumstances that exist at the beginning of the period of implementation (or, if applied to earlier periods, the beginning of the earliest period restated).

   However, lessors should not restate the assets underlying their existing sales-type or direct financing leases. Any residual assets for those leases become the carrying values of the underlying assets.

6. **GASB Statement No. 88 "Certain Disclosures related to debt, including direct borrowings and direct placements".** The primary objective of this Statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. This Statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. This Statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Future adoption of accounting pronouncements (continued)

default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses. For notes to financial statements related to debt, this Statement also requires that existing and additional information be provided for direct borrowings and direct placements of debt separately from other debt. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018 (June 30, 2019). Earlier application is encouraged.

7. **GASB Statement No. 89 "Accounting for Interest Cost Incurred before the End of a Construction Period".** The objectives of this Statement are (1) to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and (2) to simplify accounting for interest cost incurred before the end of a construction period. This Statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest cost incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type activity or enterprise fund. This Statement also reiterates that in financial statements prepared using the current financial resources measurement focus, interest cost incurred before the end of a construction period should be recognized as an expenditure on a basis consistent with governmental fund accounting principles. The requirements of this Statement are effective for reporting periods beginning after December 15, 2019 (fiscal year ended June 30, 2021). Earlier application is encouraged. The requirements of this Statement should be applied prospectively.

8. **GASB Statement No. 90 "Majority Equity Interest – and amendment of GASB Statements No. 14 and No. 61"** The primary objectives of this Statement are to improve the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018 (fiscal year ended June 30, 2020). Earlier application is encouraged. The requirements should be applied retroactively, except for the provisions related to (1) reporting a majority equity interest in a component unit and (2) reporting a component unit if the government.

9. **GASB Statement No. 91 "Conduit Debt Obligations"** The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statements achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures.

The impact of these statements on the **Office's** financial statements – cash basis, if any, has not yet been determined.

2. CASH WITH FISCAL AGENTS

Department of the Treasury of the Commonwealth of Puerto Rico

The funds of the **Office** are under the custody and control of the Secretary of the Treasury Department of Puerto Rico pursuant to Act No. 230 of July 23, 1974, as amended, known as "Commonwealth of Puerto Rico Accounting Law". The Treasury Department follows the practice of pooling cash equivalents under the custody and control of the Secretary of the Treasury. The funds of the **Office** in such pooled cash accounts are available to meet its current operating requirements.

Custodial Credit Risk

Custodial Credit Risk is the risk that, in the event of the failure of a depository financial institution, the **Office** will not be able to recover its cash and investments or will not be able to recover collateral securities that are in the possession of an outside party.

As of June 30, 2018, the Office has operating accounts with "Banco Popular of Puerto Rico" and in commingled banks accounts kept by the PR Department of the Treasury. Pursuant to Act 21 of the Commonwealth and certain of its instrumentalities that used the Governmental Development Bank of Puerto Rico (GDB) as its main depositary institution have opened accounts in private banks and have ceased depositing at the GDB. In addition, on April 28, 2017, the Financial Oversight and Management Board for Puerto Rico approved GDB's fiscal plan, as required by Public Law 114-187 Puerto Rico Oversight, Management and Economic Stability Act, also known as "PROMESA". This plan establishes an orderly winddown, financial restructuring and closing of GDB's operations.

Management has concluded that, based on facts explained above, the custodial risk on deposits in GDB is high. Notwithstanding, the PRDE concluded that the final amount of the custodial credit risk on the deposits in GDB cannot be reasonably estimated until GDB concludes its restructuring process. Deposits in commercial banks in Puerto Rico are insured up to $250,000 per institution by the FDIC; amounts in excess of the FDIC limits are collaterized by securities held by the banks.

3. COMPENSATED ABSENCES

The employees of the **Office** are classified as either civil or members of the **Office**. All employees accrue regular vacation and sick leave at 1.25 days and 1.5 days per calendar month, respectively. The allowed maximum number of accumulated days of regular vacation and sick leave is 60 days and 90 days, respectively.

During fiscal year 1997-98, the Legislature of the Commonwealth of Puerto Rico amended the Public Service Personnel Law to allow certain component units and the executive agencies of the Commonwealth to pay annually the accrued vacations and sick leave earned in excess of the limits mentioned above.

On February 4, 2017, the Government enacted Law No. 8 for the Administration and Transformation of the Human Resources of the Government of Puerto Rico. Effective on that date, this Law established and recognizes that the government is a Single Employer. Under the provisions of this law annual vacation days were reduced from thirty (30) to fifteen (15) days. The vacation days may be accumulated to a maximum of sixty (60) days.

Also, the employees hire before the effectiveness of this law, will be granted annually with eighteen (18) days of sick leave. In addition, the employees hire after the effectiveness of this law, will be granted annually with twelve (12) days of sick leave. In both cases, the sick leave days may be accumulated to a maximum of ninety (90) days.

4. PENSION PLAN

General description

The **Office** is a participating employer in a retirement plan administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). ERS covered all regular full-time public employees working for the executive and legislative branches of the Commonwealth and the municipalities of Puerto Rico (including mayors); the firefighters and police of Puerto Rico and employees of certain public corporations not having their own retirement systems. Prior to July 1, 2013, the system operated under the following benefits structures:

- Act No. 447 of May 15, 1951 ("Act 447") effective on January 1, 1952 for members hired up to March 31, 1990,
- Act No. 1 of February 16, 1990 ("Act 1") for members hired on or after April 1, 1990 and ending on or before December 31, 1999,
- Act No. 305 of September 24, 1999 (which amended Act 447 and Act 1) for members hired from January 1, 2000 up to June 30, 2013.

Employees under Act 447 and Act 1 are participants of a cost-sharing multiple employer defined benefit plan. Act 305 members are participants under a pension program known as System 2000, a hybrid defined contribution plan. Under System 2000, there was a pool of pension assets invested by the System, together with those of the current defined benefit plan. Benefits at retirement age were not guaranteed by the Commonwealth and were subjected to the total accumulated balance of the savings account.

Effective on July 1, 2013, Act No. 3 of 2013 ("Act 3") amends the provisions of the different benefits structures under the ERS. Act 3 moves all participants (employees) under the defined benefit pension plans (Act 447 and Act 1) and the defined contribution plan (System 2000) to a new defined contribution hybrid plan. Contributions are maintained by each participant in individual accounts. Credits to the individual accounts include: (1) retirement benefits accrued and savings account balances under the provisions of Act 447, Act 1 and System 2000 as of June 30, 2013; (2) contributions made by all members of ERS after June 30, 2013; and, (3) the investment yield for each semester of the fiscal year.

Benefits provided

Eligibility for retirement: Act 3 establish the following retirement eligibility requirements: (1) Act 447 regular employees upon attaining a range between 59 to 61 years (depending of date of birth) and 10 years of creditable service, (2) Act 1 employees upon attaining 55 years with 30 years of creditable service, (3) System 2000 regular employees upon attaining a range between 61 to 65 years (depending of date of birth) and, (4) Act 3 employees hired after July 1, 2013 upon reaching 67 years. High risk employees (state and municipal police, firefighters and custody officials) under Act 447 and Act 1 will be eligible at 55 years with 30 years of creditable service; for System 2000 employees at 55 years of service and for Act 1 employees hired after July 1, 2013 upon reaching 58 years.

Accrued benefits: All members are entitled to a lifetime annuity based on the balance of the deferred contribution individual account at the time of the retirement calculated based on a factor that will incorporate the individual's life expectancy and a rate of return. For Act 447 and Act 1 active participants, all retirement benefits accrued through June 30, 2013 were frozen, and thereafter, all future benefits accrue under Act 3 plan.

4. PENSION PLAN (CONTINUED)

Benefits provided (continued)

These participants will receive a pension at retirement age equivalent to what they have accrued under Act 447 and Act 1 up to June 30, 2013 plus the lifetime annuity corresponding to contributions made to the individual account after July 1, 2013 as described above. Act 447 participants, except police and mayors, may elect to coordinate coverage with Social Security benefits ("Coordinated plan"). Under this option, participants are subject to a benefit recalculation

upon attainment of the Social Security Retirement Age. For all members, if the balance of the defined contribution individual account is less than $10,000 the amount shall be paid as a lump sum instead of an annuity. Effective July 1, 2013, the minimum monthly pension amount for members who retired or disabled before July 1, 2013 is $500.

Termination benefit: Members are eligible to a lump sum payment of the defined contribution individual account as of the date of the permanent separation of service upon termination of service prior to 5 years of service or if the balance of the defined contribution individual account is less than $10,000.

Deferred retirement: Members are eligible at the applicable retirement eligibility age to a lifetime annuity based on the balance of the deferred contribution individual account plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members) upon termination of service with 5 or more years of service (10 years of creditable service for Act 447 and Act1 members) but prior to the applicable retirement eligibility, provided the member has not taken a lump sum withdrawal from the defined contribution individual account.

Death benefits: For non-retired members, their designated beneficiaries will receive a refund of the balance of the deferred contribution individual account plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members). For pensioned members retired prior to June 30, 2013, the annual income to a widow or widower or dependent children is equal to 60% of the retirement benefit payable for life for a surviving spouse or disabled children and payable until age 18 or age 25 if pursuing studies for non-disabled children. For pensioned members retired after June 30, 2013, payments to beneficiaries will be the excess, if any, of the balance of the deferred contribution individual account plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members) over the total annuity payments paid to the member and any beneficiaries.

Disability benefits: Members who are permanently separated from service due to total and permanent disability, due to disability pursuant to Act No. 127 of June 27, 1958, as amended, or due to terminal illness, as determined by the Administrator, shall be entitled to the balance of the deferred contribution individual account in a lump sum, or through the grant of an annuity, or any other optional form of payment pursuant to Section 5-110 of Act No. 447, at the option of the participant, plus the accrued benefit as of June 30, 2013 (for Act 447 and Act 1 members) at the applicable retirement eligibility age.

Beginning on June 30, 2013, no disability pensions shall be awarded pursuant to Sections 2-107 thru 2-111 of Act No. 447. A disability benefits program is established which shall provide a temporary annuity in the event of total and permanent disability. Disability benefits may be provided through one or more disability insurance contracts with one or more insurance companies authorized by the Office of the Commissioner of Insurance of Puerto Rico to conduct business in Puerto Rico. The determination as to whether a person is partially or totally and permanently disabled shall be made by the insurance company that issues the insurance policy covering the participant.

4. PENSION PLAN (CONTINUED)

Benefits provided (continued)

Special laws and pensioner additional benefits: The **Office** is required to cover other retirement benefits of its retired employees (if retired prior to July 1, 2013) as required by Commonwealth's laws, including: (1) various special laws – ad-hoc cost of living allowance adjustments (COLA) provided in prior years; (2) various special laws – additional minimum pension benefits and, (3) Act 3 retired pensioners "Additional Benefits Program". All of these other retirement benefits are applicable only to employees who retired prior to July 1, 2013 under Act 447 and Act 1. The "Additional Benefits Program" includes: (1) a medication bonus of $100 per member which shall be paid no later than July 15 of each year; (2) a Christmas bonus of $200 per member which shall be paid no later than December 20 of each year and, (3) a matching share of $1,200 for healthcare insurance plan. These healthcare benefits are provided through insurance companies whose premiums are paid by the retired employees with the matching share financed by the **Office**.

Retirement systems reform

Act No. 106 of August 23, 2017 ("Act 106") was enacted to reform the Commonwealth retirement systems and, among other dispositions, provide the necessary legal and operational structure of the determination and payment of accrued pension benefits as of June 30, 2017, the creation and transition to a new defined contribution plan and the reform of ERS's governance and administration, effective on July 1, 2017. Those dispositions are summarized as follows:

Determination of accrued pension benefits as of June 30, 2017 and payments

Effective July 1, 2017 participants ceased to accrue new pension benefits and are no longer able to make direct credit payments or to make additional contributions to the ERS. The ERS created and will maintain, for each participant or actual beneficiary, an individual record as of June 30, 2017 which includes the accrued pension benefits, employment history and accumulated contributions made. All benefits including retirement, disability, death, and other pensioner additional benefits were determined in accordance to the specific benefit structures under Act 447, Act 1, Act 305 and Act 3 and will be paid based on the information provided in the individual record. The accrued pension benefits will be funded through:

- The net proceeds of the sale of ERS's assets,
- A pay-as-you-go ("PayGo") charge to the participant employers determined by ERS and billed by the P.R. Department of Treasury ("PRDT"),
- Commonwealth's legislative expenditure appropriations,
- Donations by any public or private entity,
- 25% of first or periodic payments on public-private partnership contracts,
- Other funds determined by the Commonwealth's Legislature.

4. PENSION PLAN (CONTINUED)

Determination of accrued pension benefits as of June 30, 2017 and payments (continued)

On June 27, 2017 the PRDT issued the Circular Letter No. 1300-46-17 to communicate to the Commonwealth, the Municipalities and other participants of the ERS the conversion procedures to a new PayGo model, effective on July 1, 2017. Under the PayGo funding, the participant employers directly pay the pension benefits (including other special laws and additional pensioner benefits) as they are due rather than attempt to build up assets to pre-fund future benefits. This funding method allows the retirement systems to continue to pay benefits even after the plans' assets have been exhausted. In addition, as a result of the implementation of PayGo funding, employers' contributions related to additional uniform contributions were eliminated. Payments are made by the employers (the Agency) through a government treasury single account (TSA) maintained on a separate trust under the custody of PRDT. TSA funds are deposited and maintained in a private commercial bank. It is expected that, as the ERS's assets become depleted, the PayGo charge will increase. On July 20, 2017 ERS sold investments for approximately $297 million.

Act 106 includes penalties and specific procedures for collection of unpaid PayGo charges. Each beneficiary, participant or pensioned will have personal collection rights against every incumbent, head of agency, director of budget or finance or any officer with responsibility at government, public enterprise or municipality to claim unpaid contributions starting on the effective date of the Act and demand that they be paid as required.

Creation and transition to a new defined contribution plan

General - Effective July 1, 2017, a new defined contribution plan ("DC Plan") is created and maintained in a separate trust. It covers all active participants of the ERS as of that date and participants enrolled in the public service after that date. The Retirement Board (as discussed later) is responsible for oversight of the DC Plan; the PRDT currently serves as the trustee and custodian of the DC Plan's assets, which are deposited in a private bank account.

The transition to the new DC Plan is currently in process. In accordance with Act 106 requirements, the Retirement Board is evaluating proposals to appoint a plan administrator which will perform recordkeeping and management functions for the DC Plan, including the development and adoption of a plan document, effective July 1, 2019. The transition includes the creation of a separate trust and the transfer of participant accounts.

Participant accounts and contributions - Funds are maintained in individual accounts for each participant which are credited with participant's pre-tax contributions and investment earnings. Participants are required to contribute at least 8.5% of gross salary. The Plan provides for voluntary additional pre-tax contributions as permitted by the Puerto Rico Internal Revenue Code of 2011 ("2011 PR Code"). After July 1, 2019, participants may direct the investment of their contributions into various investment options offered by the DC Plan.

Payment of benefits - Upon termination of service a participant or the participant beneficiaries may elect to receive an amount equal to the value of the participant's interest in his or her account in a lump-sum amount, maintain his or her account in the DC Plan, or roll-over their account to a qualified plan under the 2011 PR Code. Upon participant's death the account balance will be distributed to its designated beneficiaries. Distributions are subject to income tax in accordance with the provisions of the 2011 PR Code. For participants of the DC Plan with accrued pension benefits as of June 30, 2017, benefits will include amounts participant's interest in his or her account plus accrued pension benefits funded through the PayGo system.

4. PENSION PLAN (CONTINUED)

Reform of ERS's governance and administration

Act 106 creates a Retirement Board composed of thirteen (13) members (government officials, representatives of teachers, judicial system, public corporations and mayors) which replaces the Board of Trustees and perform overall governance of all retirement systems, including ERS, the Teachers and Judiciary Retirement Systems. ERS's employees that are not retained under the new administrative structure will be transferred to public agencies in conformity to Act No. 8 of 2017.

Pension liabilities, pension expense, and deferred outflows/inflows of resources related to pensions; other required disclosures under GASB Statement No. 73

As discussed above, pursuant to Act 106, participants ceased to accrue new pension benefits and are no longer able to make direct credit payments or to make additional contributions to the ERS. In addition, benefit payments are made through a PayGo funding system, a TSA account under the custody of PRDT and maintained in a separate trust fund. Plans operated under various benefit structures prior to July 1, 2017 are administered by the new Retirement Board through a trust fund that do not meet the requirements of **GASB Statement No. 68** as of July 1, 2017. Instead, the employers may be subject to the requirements of **GASB Statement No. 73**, "Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68".

5. TERMINATION BENEFITS

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

For eligible employees that choose the economic incentives and have at least 30 years of credited service and the age for retirement or have the age for retirement, the **Office** will make the employee and the employer's contributions to the Retirement System for a five year period. Additionally, eligible employees that choose to participate in the early retirement benefit program of that choose the economic incentive and have less than 15 years of credited service are eligible to receive health plan coverage for up to 12 months in a health plan selected by the management of the **Office**. The total number of employees who were voluntary terminated was five (5).

6. COMMITMENTS AND CONTINGENCIES

Federal grants

The **Office** participates in a Federal Grant Program. This program is subject to financial and compliance audits. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the **Office** expects such amounts, if any, not to be material.

Claims and lawsuits

The Commonwealth of Puerto Rico Law No. 104 of June 30, 1955, as amended, known as Claims and Lawsuits against the State provide that lawsuit initiated against an agency or instrumentality of the Commonwealth of Puerto Rico, present and former employers, directors, mayors and others may be represented by the Department of Justice of the Commonwealth of Puerto Rico. Any adverse claims to the defendants are to be paid by the Commonwealth of Puerto Rico General Fund. However, the Secretary of the Treasury of the Commonwealth of Puerto Rico has the discretion of requesting reimbursement of the funds expended for these purposes form the public corporations, governmental institutions and agencies of the defendants. No payments for asserted or unasserted claims, if any, has been represented in the accompanying financial statement.

7. GOING CONCERN – PRIMARY GOVERNMENT

The Commonwealth currently faces a severe fiscal, economic and liquidity crisis, the culmination of many years of significant governmental deficits, a prolonged economic recession (which commenced in 2006), high unemployment, population decline, and high levels of debt and pension obligations. Further stressing the Commonwealth's liquidity is the vulnerability of revenue streams during times of major economic downturns and high health care, pension and debt service costs. As the Commonwealth's tax base has shrunk and its revenues affected by prevailing economic conditions, health care, pension and debt service costs have impacted significant portion of the General Fund budget, which has resulted in reduced funding available for other essential services, like the **Office**, which is part of the Commonwealth.

Considering that the **Office** is significantly dependent on the funds received from the Commonwealth to match the federal awards and comply with the levels of effort required by federal regulations, the limitation of the Commonwealth to meet its obligations on a timely manner, may have an effect on the **Office**'s operations in the near term.

The following is a summary of relevant laws enacted and actions taken to address the Commonwealth's fiscal crisis:

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

7. GOING CONCERN – PRIMARY GOVERNMENT (CONTINUED)

On January 18, 2017 (Act No. 2 of 2017), the Puerto Rico Fiscal Agency and Financial Advisory Authority Act, was enacted to expand FAFAA's powers and authority (as initially established under the Moratorium Act) so that FAFAA has the sole responsibility to negotiate, restructure, and reach agreements with creditors on all or part of the public debt or any other debt issued by any Commonwealth entity. FAFAA is also responsible for the collaboration, communication, and cooperation efforts between the Commonwealth and the Oversight Board under PROMESA. In addition, Act No. 2 of 2017 established FAFAA as the Commonwealth entity responsible for carrying out the roles inherited from the GDB along with additional duties and powers, which include, among other things: (i) oversight of the Commonwealth budget; (ii) an administrative presence on every board or committee where the GDB president is currently a member; (iii) authority to conduct audits and investigations; and (iv) authority to freeze budgetary items, appoint trustees, redistribute human resources, and change procedures.

On January 26, 2017 (Act No. 4 of 2017) introduced several human-capital and labor reforms to improve Puerto Rico's competitiveness and foster economic development, while relaxing legal requirements for hiring and retaining employees. Specifically, Act 4 No. of 2017 (i) established lower accrual rates for both vacation days and sick leave, (ii) approximately doubled work hours required for accrual of Christmas bonuses, (iii) placed a $600 cap on Christmas bonuses, and (iv) reduced severance pay for unjust termination, among other reforms.

On January 29, 2017 (Act No. 5 of 2017), the Puerto Rico Fiscal Responsibility and Financial Emergency Act, was enacted to maintain the moratorium on debt payment existing under the Moratorium Act; however, it allowed the Commonwealth to segregate funds that would eventually be used to fund the payment of public debt. Act No. 5 of 2017 states that the Governor may pay debt service as long as the Commonwealth is able to continue to fund essential services, such as the health, safety, and well-being of the people of Puerto Rico, including providing for their education and assistance to residents. Act No. 5 of 2017 continued to declare the Commonwealth to be in a state of emergency and increased the Governor's powers to manage the Commonwealth's finances. The emergency period under Act No. 5 of 2017 was set to expire on May 1, 2017 to coincide with the expiration of the Title IV Stay (as discussed above), unless extended by an additional three months by executive order. On April 30, 2017, the Governor issued executive order OE-2017-031, which extended to the Act No. 5 of 2017 emergency period to August 1, 2017. On July 19, 2017, the Legislature enacted Act No. 46 of 2017, which further extended the Act No. 5 of 2017 emergency period through December 31, 2017. Act No. 46 of 2017 allowed the Governor to sign executive orders to extend the emergency period for successive periods of six months as long as the Oversight Board remains established for Puerto Rico under PROMESA.

On February 4, 2017 (Act No. 8 of 2017), known as the Single Employer Act, was enacted to merge public agencies to establish the government as a single employer. This legislation is designed to facilitate employee transfers between the Commonwealth's 118 agencies, which prior to the enactment of Act No. 8 of 2017, these agencies operated as separate employers, with different administrative divisions and wages for the same occupations.

On February 8, 2017 (Act No. 9 of 2017) and Act No. 14 of February 21, 2017 (Act No. 14 of 2017) introduced a series of tax amendments to provide incentives to professionals to stay in Puerto Rico by promoting and facilitating the creation and management of retirement plans and other trusts to promote financial stability and job creation.

On April 29, 2017 (Act No. 26 of 2017), known as the Fiscal Plan Compliance Act, introduced a series of changes and freezes to existing public employees' labor bargaining agreements, reductions and eliminations to previously granted public employee benefits, and other fiscal control measures geared toward compliance with the government expenditures cuts and savings.

8. HURRICANES IRMA (DR-4336) AND MARIA (DR-4339)

From September 5, 2017 through September 7, 2017, Puerto Rico suffered the passing of Hurricane Irma, a Category 4 hurricane that severely affected the municipal islands of Vieques and Culebra and several municipalities located in the metro, north, east and south areas of the Island: Adjuntas, Aguas Buenas, Barranquitas, Bayamón, Camuy, Canóvanas, Carolina, Cataño, Ciales, Comerío, Dorado, Guaynabo, Gurabo, Hatillo, Jayuya, Juncos, Las Piedras, Loíza, Luquillo, Naguabo, Orocovis, Patillas, Quebradillas, Salinas, San Juan, Utuado, Vega Baja and Yauco. It was declared a major disaster area by the President of the United States on September 10, 2017 and almost $3.9 million dollars in public assistance grants have been obligated.

Just two weeks after Hurricane Irma, on September 17, 2017, Hurricane María hit Puerto Rico as a Category 4 hurricane, causing catastrophic damages to the infrastructure and the collapsing of the electric power grid and the telecommunications system of the entire Island. It was declared a major disaster area by the President of the United States on September 20, 2017 and approximately $508 million dollars in public assistance grants have been obligated. Many citizens lost their homes and the business sector suffered heavy losses due to infrastructure damages, looting during and after the hurricane, loss of inventory and the absence of electric power, which forced businesses to invest in power generators to operate, incurring in significant gasoline and diesel expenses.

9. SUBSEQUENT EVENTS

Subsequent events were evaluated through October 31, 2019, the date the financial statements were available to be issued. No significant events that should have been recorded or disclosed in the financial statements, except as noted in the following paragraph.

Funds Designated to the Department of Housing of the Government of Puerto Rico

On July 27, 2018 Law 162 amends Article 4.1 of Law 10-2017, as known Organic Law of “Oficina de Desarrollo Socioeconómico Comunitario”(ODSEC) which indicates that the Department Housing of the Government of Puerto Rico will be the entity designated to receive and administer the “Community Development Grant” (CDBG) funds, the special funds included in the CDBG program that include the “Community Development Block Grant for Disaster Recovery (CDBG-DR), the Neighborhood Stabilization Program” (NSP), “Disaster Recovery” and the funds under the Section 108 Loan Program, known as the “Loan Guarantee Assistance Under Section 108”.

GDB Qualifying Modification under Title VI of PROMESA

On March 23, 2018, The Governmental Development Bank for Puerto Rico (GDB) ceased its operations. Also, on November 29, 2018, GDB completed a restructuring of certain of its indebtedness pursuant to a Qualifying Modification under Title VI of PROMESA (the Qualifying Modification).

	Budgeted Amounts			
	Original Budget	Final Budget	Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
CASH RECEIPTS				
Appropriations from the Commonwealth of Puerto Rico:	$ 2,986,000	$ 2,893,000	$ 2,893,000	$ -
Total cash receipts	2,986,000	2,893,000	2,893,000	-
CASH DISBURSEMENTS AND ENCUMBRANCES				
Payroll and fringe benefits	2,043,000	1,943,000	1,634,578	308,422
Professional services	264,000	186,000	144,950	41,050
Equipments	3,000	10,000	4,000	6,000
Supplies and materials	26,000	36,000	14,560	21,440
Permanent improvements	500,000	500,000	97,356	402,644
Utilities	120,000	166,000	82,140	83,860
Transportation	20,000	31,000	26,163	4,837
Others	10,000	21,000	8,873	12,127
Total cash disbursements and encumbrances	2,986,000	2,893,000	2,012,620	880,380
Excess (deficiency) of cash receipts over (under) cash disbursements and encumbrances	$ -	$ -	$ 880,380	$ 880,380

See notes to Budgetary Comparison Schedule.

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

On January 2, 2017, the Governor of Puerto Rico signed the Executive Order No. 2017-005, which required that all departments, agencies, and instrumentalities of the Government of Puerto Rico and those expressly required by the Governor, are ordered to implement the Zero-Base Budget methodology for the preparation of the budget for fiscal year 2017-2018 and subsequent fiscal years, per the applicable techniques and approaches of Zero- Base Budget and should be in conformity with the Fiscal Plan approved by the Oversight Board for Puerto Rico, pursuant to the Federal Law Pub. L. 114-187, *Puerto Rico Oversight, Management and Economic Stability Act* (PROMESA).

The revenues recognized in the General fund consist of appropriations from the Office of Management and Budget of the Commonwealth of Puerto Rico for recurrent and ordinary functions of Office. The procedures followed in approving the annual budget is as follows:

1. Between November and December **Office** submits to the Office of Management and Budget of the Commonwealth of Puerto Rico an operating budget petition for the fiscal year commencing the following July 1.

2. At the beginning of the ordinary session of the Legislative Assembly of the Commonwealth of Puerto Rico, the Governor submits a proposed budget for the fiscal year covering the whole operations of the Commonwealth. This proposed budget includes estimated expenditures and the means of financing them.

3. The annual budget is legally enacted through the approval by the Legislative Assembly of the Joint Resolution of the General Budget. Subsequently to enactment, the Office of Management and Budget of the Commonwealth has the authority to make the necessary adjustments to the budget.

4. Beginning with fiscal year 2018-2019 the budget procedure to be used for the confection of the budget must be the methodology of Zero-Base budgeting.

The financial statement is presented at the programmatic level. However, budgetary control and accounting are maintained at a level more detailed to provide the management control in detail of the expenses to the appropriate level of the budget.

The budget is adopted in accordance with a budgetary basis of accounting which differs from USGAAP. The Commonwealth of Puerto Rico Department of Treasury and the Office of Management and Budget have the responsibility to ensure that budgetary spending control is maintained on an individual appropriation account basis. Budgetary control is exercised through the PRIFAS Accounting System.

Federal Grantor/ Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Grant ID/Pass-Through Identification Number	Passed Through to Subrecipients	Total Federal Expenditures
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:				
Community Development Block Grant/State's Program (State administered small cities program)	14.228			
FY 2017 CDBG Program		B17DC720001	$ 285,101	$ 385,271
FY 2016 CDBG Program		B16DC720001	2,837,963	3,570,527
FY 2015 CDBG Program		B15DC720001	1,934,090	1,934,090
FY 2014 CDBG Program		B14DC720001	1,072,253	1,072,253
FY 2013 CDBG Program		B13DC720001	542,944	555,627
FY 2012 CDBG Program		B12DC720001	697,447	697,447
FY 2011 CDBG Program		B11DC720001	496,707	497,467
FY 2010 CDBG Program		B10DC720001	571,924	571,924
FY 2009 CDBG Program		B09DC720001	62,221	62,221
FY 2008 CDBG Program		B08DC720001	2,828	2,828
FY 2011 CDBG Program – Neighborhood Stabilization Program (HERA) (NSP1)		B11DN720001	21,752	21,752
FY 2008 CDBG Program – Neighborhood Stabilization Program (HERA) (NSP1)		B08DN720001	44,058	44,058
FY 2008 CDBG Program-Disaster Recovery		B08DI720001	1,336,806	1,336,806
Total US Department of Housing and Urban Development			**9,906,094**	**10,752,271**
U.S. DEPARTMENT OF JUSTICE				
Juvenile Justice and Delinquency Prevention-allocation to State (States Formula Grant)	16.540	2015JFFX0081	-	22,900
		2015JFFX008	9,300	10,242
		2013MUFX041	-	18,525
Total Juvenile Justice and Delinquency Prevention-allocation to State (States Formula Grant)			9,300	51,667
Total U.S. Department of Justice			**9,300**	**51,667**

Federal Grantor/ Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Grant ID/Pass-Through Identification Number	Passed Through to Subrecipients	Total Federal Expenditures
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES				
Community Services Block Grant	93.569			
FY 2018CSBG Program		G18-B1PRCOSR	8,985,962	8,985,962
FY 2017CSBG Program		G17-B1PRCOSR	15,404,196	16,035,065
FY 2016CSBG Program		G16-B1PRCOSR	1,084,718	1,087,055
Total U.S. Department of Health And Human Services			**25,474,876**	**26,108,082**
TOTAL EXPENDITURES OF FEDERAL AWARDS			**$ 35,390,270**	**$ 36,912,020**

See notes to Schedule of Expenditures of Federal Awards.

GENERAL

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the funds expended by the **Socioeconomic and Community Development Office (Office)** from all federal programs for the year ended June 30, 2018. The **Office's** reporting entity is defined in **Note 1** to the financial statements.

BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards is presented in accordance with the requirements of *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance)*. Therefore, some of the amounts presented in the Schedule may differ from the amounts presented in, or used in the presentation of, the basic financial statements. Because the Schedule presents only a selected portion of the operations of the **Office**, it is not intended to and does not present the financial position and changes in net position of the **Office**.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures presented on the Schedule are reported on the cash basis of accounting. Expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

The Catalog of Federal Domestic Assistance (CFDA) Number is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence. State or local government redistributions of federal awards to the Agency, known as "pass–through awards", should be treated by the Agency as though they were received directly from the federal government. The Uniform Guidance requires the schedule to include the name of the pass–through entity and the identifying number assigned by the pass-through entity for the federal awards received as a sub recipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

RECONCILIATION TO FINANCIAL STATEMENTS

Information reported in the accompanying Schedule of Expenditures of Federal Awards agreed with or has being reconciled to the information reported in the **Office's** basic financial statements as follows:

Community Service Block Grant Fund	$ 26,108,082
Community Service Block Grant Fund	10,752,271
Juvenile Justice and Delinquency Prevention – Allocation to State	51,667
Total	**$ 36,912,020**

INDIRECT COST RATE

The **Office** has elected not use the 10% de minimis cost rate, and did not charge indirect cost to federal grants during the year ended June 30, 2018.

López-Vega, CPA, PSC
Certified Public Accountants / Management Advisors

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

To the Executive Director
Commonwealth of Puerto Rico
Socioeconomic and Community Development Office
San Juan, Puerto Rico

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States of America, the financial statement of the **Socioeconomic and Community Development Office (the Office)**, as of and for the year ended June 30, 2018, and the related notes to the financial statement, which collectively comprise the **Office's** financial statements as listed in the table of contents, and have issued our report thereon dated October 31, 2019.

Emphasis of Matters

Uncertainty about Ability to Continue as a Going Concern – Primary Government

The accompanying financial statements of the **Office** have been prepared assuming that the Commonwealth will continue as a going concern. As discussed in **Note 7** to the financial statements, the Commonwealth's recurring deficits, negative financial position, further deterioration of its economic condition, and inability to access the credit markets raises substantial doubt about the Commonwealth's ability to continue as a going concern. Management's plans regarding these matters are also described in **Note 7**. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinions are not modified with respect to this matter.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs, as item **2018-001** and **2018-002** that we consider to be material weaknesses.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether **Office's** financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items **2018-001** to **2018-004.**

Purpose of this Report

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

López-Vega, CPA, PSC

LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
October 31, 2019
Stamp No. 2758861 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

López-Vega, CPA, PSC
Certified Public Accountants / Management Advisors

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

To the Executive Director
Commonwealth of Puerto Rico
Socioeconomic and Community Development Office
San Juan, Puerto Rico

Report on Compliance for Each Major Federal Program

We have audited the **Socioeconomic and Community Development Office (Office)** compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have direct and material effect on each of the **Office's** major federal programs for the year ended June 30, 2018. The **Office's** major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditors' Responsibility

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

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

Opinion on Each Major Federal Programs

In our opinion, the **Office** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2018.

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

Other Matters

The results of our auditing procedures disclosed an instance of noncompliance, which is required to be reported in accordance with the Uniform Guidance and which is described in the accompanying schedule of findings and questioned costs as Item **2018-003** and **2018-004**. Our opinion on each major federal program is not modified with respect to this matter.

Office's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. **Office's** response was not subject to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control over Compliance

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

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

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

Office's response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. **Office's** response was not subject to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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

Report on Internal Control over Compliance (continued)

However, we identified certain deficiencies in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item **2018-003** and **2018-004** that we consider to be significant deficiencies.

Office's response to the interval control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. **Office's** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of this Report

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

López-Vega, CPA, PSC

LOPEZ-VEGA, CPA, PSC
San Juan, Puerto Rico
October 31, 2019
Stamp No. 2758862 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.

Section I – Summary of Auditors' Results

Financial Statement

Opinion Unit	Type of Opinions
General Fund	Unmodified
Community Services Block Grant – Federal	Unmodified
Community Development Block Grant – Federal	Unmodified
Others Funds	Unmodified

Internal control over financial reporting:		
Material weakness(es) identified?	Yes ☒	No ☐
Significant deficiency(ies)?	Yes ☒	No ☐
Noncompliance material to financial statements noted?	Yes ☐	No ☒

Federal awards

Internal Control over major programs:		
Material weakness(es) identified?	Yes ☐	No ☒
Significant deficiency(ies)?	Yes ☒	No ☐
Type of auditors' report issued on compliance for major programs:	Qualified	
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200 section 200.516 (a) of the Uniform Guidance?	Yes ☐	No ☒

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
93.569	Community Services Block Grant

Dollar threshold used to distinguish between Type A and Type B programs	$ 1,107,361	
Auditee qualified as low-risk auditee?	Yes ☐	No ☒

Section II – Financial Statement Findings

Finding Reference	**2018-001**
Requirement	**Financial Reporting- Accounting Records**
Type of finding	**Material weakness (MW), Instance of Noncompliance (NC)**
Statement of Condition	The **Socioeconomic and Community Development Office (Office)** does not maintain monthly reconciliations with the transaction reported on the GL-1292 as kept by the Department of Treasure, entity that controls the office's budget and accounting in the PRIFAS accounting system. Also, the **Office** did not maintain an accounting that summarizes the transactions of all of its General Ledger format in order to properly record cash receipts, cash disbursements and obligations for the transactions of all of its Governmental Funds (Local, State and Federal funds).
Criteria	Law 230 of July 23, 1974, as amended, states that the accounting system will be designed in a manner which provides clear and complete information of the results of the financial operations. Also, the accounting system should provide reliable reports for the preparation and justification of the budget needs and to control the budget execution which constitute an effective control over the revenues, expenditures, funds, property and other assets.
Cause of Condition	The **Office** did not establish effective internal controls to maintain monthly reconciliations with the transactions reported on the GL-1292 as kept by the department of treasury.
Effect of Condition	The **Office's** accounting system did not provide updated and complete financial information that present the financial position and the result of operations. Such information is necessary to take management decisions.
Recommendation	We recommend that the **Office's** management should implement internal control and procedures in order to maintain an accounting system that contains information pertaining to all transactions.
Questioned Costs	None

Section II – Financial Statement Findings

Finding Reference	**2018-002**
Requirement	**Payroll and Related Liabilities – Personnel, Employment, Rate authorizations and Timekeeping**
Type of finding	**Material Weakness in Internal Control (MW), Instance of Noncompliance (NC)**

Statement of Condition

During our test, we examined twenty (20) employee files as of June 30, 2018, the assistance time cards and the accrue vacation cards; after procedures performed we noted the following:

a) In thirteen (13) cases, the supervisors of the different divisions did not perform the annual employee's evaluations.

b) In seven (7) cases, the "Drug Free Workplace Act" agreement including the signature of the **Office** employees certifying their knowledge of the compliance with this requirement were not available for our examination.

c) In five (5) cases we did not find the Employment Eligibility Verification (I-9) in the employee file.

d) In two (2) cases the Employment Eligibility Verification (I-9) does not contain the employee identification information and was not signed by the employer or authorized representative.

e) In six (6) cases we did not find the direct deposit authorization in the employee's files.

f) In one (1) case we did not find the Employee's Withholding Allowance Certificate (W-4) in the employee file.

g) In one (1) case, the employee's time assistance cards do not agree with the balance presented in the Accumulated Sick Leave Vacation Report submitted to the Department of Treasury as 6/30/2018.

h) In one (1) case we did not find the evidence of the cancelled checks.

Criteria

Law 184 from August 3, 2004 for the Administration of Human Resources in the Public Services states the controls and procedures required to be maintained over the documentation that supports the employment of personnel and to evaluate the efficiency of the jobs performed by them.

Section II – Financial Statement Findings

Finding Reference	**2018-002 (Continued)**
Cause of Condition	The internal control procedures failed to assure the proper preparation and payment of payroll and the correctness of accumulative vacation and sickness balances in these cases.
Effect of Condition	The **Office** did not maintain an adequate control over these personnel files and the compensated absences cards. Also, the **Office** did not comply with regulations stated Law 184 from August 3, 2004 for the Administration of Human Resources in the Public Service.
Recommendation	We recommended the Human Resources Division Director the following: a) Establish adequate procedures which require all division supervisors perform periodic evaluations. b) To review that all the employees are informed about the "Drug-free Workplace Act". The division must maintain evidence supporting that a copy of the mentioned regulation was provided to the employees. c) The employee in charge to custody the employee files must verify periodically that all employee files include all required documentation. d) That the Accumulated Sick Leave Vacation Report submitted to the Department of Treasury agrees to the employee's time assistance cards.
Questioned Costs	None

Section III-Major Federal Award Program Finding and Questioned Costs

Finding Reference	**2018-003**
Federal Agency	**U.S. Department of Health of Health and Human Services**
Federal Program Title	**Community Services Block Grant (CFDA No. 93.569)**
Compliance Requirement	**Subrecipient Monitoring (M)**
Type of finding	**Significant Deficiencies in Internal Control (SD)** **Instance of Noncompliance (NC),**
Statement of Condition	We performed audit procedures to the four (4) sub-recipient monitoring reports and noted that for one (1) sub-recipient of the **Office's** did not realize monitoring procedures.
Criteria	42 USC 9914 (a)(1)(2), establishes that (a) In order to determine whether eligible entities meet the performance goals, administrative standards, financial management requirements, and other requirements of a State, the State shall conduct the following reviews of eligible entities:(1) a full onsite review of each such entity at least once during each 3-yearperiod, (2) an onsite review of each newly designated entity immediately after the completion of the first year in which such entity receives funds through the Community Services Block Grant program (CSBG).
Cause of Condition	Internal Control Monitoring Program for Federal Funds CSBG establishes the guidelines over monitoring reports. The **Office** does not have sufficient staff to perform monitoring reviews to sub-recipients.
Effect of Condition	The **Office** cannot ensure that the delegated funds to the sub-recipients are being used to meet the goals and standards required by the State. Also, the **Office** is not in compliance with the 42 USC 9914 (a)(1)(2).
Recommendation	**Office** should strengthen internal control procedures in supervision process of the monitoring are to comply with state and federal regulations.
Questioned Cost	None

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	**2018-004**
Requirement	**Single Audit Act**
Type of Finding	**Significance Deficiency (SD), Instance of Noncompliance (NC)**
Statement of Condition	The Single Audit Report for the fiscal year ended June 30, 2018 was not issued within nine (9) months after the end of the audit period. significant deficiencies
Criteria	The Single Audit Act, as amended, requires that the audit report must be submitted to the Federal Audit Clearinghouse no later than nine (9) months after the end of the audit period.
Cause of Condition	The Agency did not comply with the established regulation as prescribed in OMB Super Circular Uniform Guidance.
Effect of Condition	The Agency could lose federal grants due to the noncompliance with the Single Audit Act requirements.
Recommendation	Procedures should be implemented to ensure that the Agency complies with the established Federal Regulation, as prescribed by OMB Super Circular Uniform Guidance.
Questioned Costs	None

GOVERNMENT OF PUERTO RICO
Office for the Socioeconomic and
Community Development of PR

PUERTO RICO COMMUNITY SERVICES BLOCK GRANT

Corrective Action Plan
For Fiscal Year Ended June 30, 2018

Audit Report on Compliance and Internal Control 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

Audit Period: July 1, 2017 to June 30, 2018

Fiscal Year: 2017-2018

Original Finding Number	Statement of Concurrence or Nonconcurrence	Corrective Action
2018-01	The Office for the Socioeconomic and Community Development of Puerto Rico (ODSEC) does not maintain monthly reconciliations with the transaction reported on the GL-1292 as kept by the Department of the Treasury, entity that controls the Office's budget and accounting in the PRIFAS Accounting System. Also, the Office did not maintain an accounting that summarizes the transactions of all its General Ledger format in order to properly record cash receipts, cash disbursements and obligations for the transactions of all its Governmental Funds (Local State and Federal Funds).	ODSEC agrees with the audit recommendation. We acknowledge the importance of documented policies and procedures in demonstrating sound internal controls. ODSEC's Administration is in the process of procuring an external and independent consultant that will assist in the creation of a revised and updated Policies and Procedures Manual for all financial reporting matters. This include comprehensives instruction in accounting procedures under the current Accounting System, as well as updates to all non-routine transactions. This task is expected to be completed by March 31, 2020.

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Oficina para el Desarrollo Socioeconómico y Comunitario

2018-02	During our test, we examined twenty (20) employee's files as of June 30, 2018, the assistance time cards and the accrue vacation cards, after procedures performed, we noted the following: a) In thirteen (13) cases, the supervisors of the different divisions did not perform annual employee's evaluations. b) In seven (7) cases, the Drug Free Workplace Act Agreement, including the signature of the Historic Preservation employee's certifying their knowledge of the compliance with the requirement, were not available for our examination. c) In five (5) cases, we did not find the Employment Eligibility Verification in the employee's file. d) In two (2) cases, the Employment Eligibility Verification (I-9) does not contain the employee's identification and was not signed by the employer or authorized representative. e) In six (6) cases, we did not find the direct deposit authorization in the employee's file. In one (1), we did not find the Employees' Withholding Allowance Certificate (W-4) in the employee's file. f) In one (1) case, the employee's time assistance cards do not agree with the balance presented in the Accumulated Sick Leave Vacation Report submitted to the Department of Treasury as of June 30, 2018. g) In one (1) case, we did not find the evidence of the cancelled checks.	ODSEC Management agrees with the recommendations from the auditors. Further, a review is being made of the types of errors found as the underlying processes and procedures. Based on this information, additional communication and training is being provided to the appropriate staff in the Human Resources Division to facilitate the timely and accurate posting of payroll and payroll benefits, and so that errors can be found and corrected on a monthly basis at a minimum. Completion Date: December 31, 2019.

2018-03	Federal Agency: Community Services Block Grant (CFDA No. 93-569) Subrecipient Monitoring (M) Significant Deficiencies in the Internal Control (SD) Instance of not compliance We performed audit procedures to the four (4) Sub-Recipient Monitoring Reports and noted that for one (1) Sub-Recipient the Office's did not realize monitoring.	The Office for the Socioeconomic and Community Development of Puerto Rico (ODSEC) established the Monitoring Unit within the CSBG Administration in October of 2018 and it became fully functional at once, with its primary responsibility to perform Sub-Recipient Monitoring for CSBG Programs administered by ODSEC. Accordingly, three (3) of the four (4) CSBG Subrecipients Monitoring Reviews are been finalized and one (1) is in process and is expected to be completed by December 31, 2019.
2018-04	Single Audit for Fiscal Year 2016-2017 has not yet been submitted at the time of the Single Audit of Fiscal Year 2017-2018.	The Office for the Socioeconomic and Community Development of Puerto Rico (ODSEC) agrees with the finding. The ODSEC has since improved the internal tracking process to ensure Federal Financial Status Reports are submitted on a timely basis in accordance with grant(s) reporting schedule. Due to budgetary limitations, the state does not anticipate investing in software, for the time being, to allow for the in-house preparation of the full financial statements and notes; however, certain entries to convert individual fund activity to government wide statements were started during 2017 Fiscal Year and will be completely done in-house for the 2020 Fiscal Year.

CERTIFY BY: Raymond Vega Clemente
Name

EXECUTIVE DIRECTOR: ____________
Signature

DATE: 31 de octubre de 2019

Single Audit for fiscal year 2016-2017 has not been submitted as of October 31, 2019, the date in which the Single Audit of fiscal year 2017-2018 was issued.