

**SOLID WASTE AUTHORITY
(A Component Unit of the
Commonwealth of Puerto Rico)**

**BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2012 AND
INDEPENDENT AUDITORS' REPORT**

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2012 AND
INDEPENDENT AUDITORS' REPORT

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INDEPENDENT AUDITORS' REPORT

Secretary of the Department of
Natural and Environmental Resources
Commonwealth of Puerto Rico
Solid Waste Authority
San Juan, Puerto Rico

We have audited the accompanying basic financial statements as listed in the table of contents of the Solid Waste Authority (the Authority), a component unit of the Commonwealth of Puerto Rico, as of and for the year ended June 30, 2012. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Authority as of June 30, 2012, and the changes in its net assets, and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in note 16 to the financial statements, the beginning balance of net assets has been restated to correct certain accounting errors belonging to prior years.

The Management's Discussion and Analysis on pages 3 through 10 is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The combining statement of revenues, expenses and changes in net assets is presented for purposes of additional analysis and is not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

San Juan, Puerto Rico
March 6, 2013

Ortiz, Rivera, Rivera & Co.

The stamp E52624 was affixed to the original of this report.



ORTIZ, RIVERA², RIVERA & CO.

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SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

Our discussion and analysis of the Solid Waste Authority (the Authority) financial performance provides an overview of the Authority's financial activities for the fiscal year ended June 30, 2012, please read it in conjunction with the Authority's audited basic financial statements.

FINANCIAL HIGHLIGHTS:

1. The Authority experienced a decrease in its net assets of \$1,501,353 or 84 % during the current fiscal year. This change is mostly related to an increase in the revenues from contracts of approximately \$240,344, a decrease in the voluntary retirement benefits of approximately \$2,774,706 (enacted act No. 70), and a decrease in the depreciation expenses of \$184,211 or -3%. The Authority also experienced a decrease in general and administrative expenses of approximately \$577,054 or -17% and an increase in the economic assistance programs provided to the municipalities on \$1,653,578 (73%) 2011-2012.
2. The Authority's assets exceeded liabilities by \$78,434,970 as of June 30, 2012.
3. The Authority's unrestricted net assets increased by \$5,293,865 or 1,617% during the current fiscal year.
4. Operating expenses decreased by \$1,048,884 or -5%, basically due to a decrease in voluntary retirement benefits resulting from the Commonwealth enacted Act No. 70 to establish a program that provides benefits for early retirement or economic incentives for voluntary employment terminations to eligible employees, as defined, including employees of the Authority and Economic Assistance Programs during fiscal year 2011-2012.

USING THE ANNUAL REPORT:

This annual report consists of a series of basic financial statements. The (i) Statements of Net Assets, (ii) the Statements of Revenues, Expenses and Changes in Net Assets, (iii) the Statements of Cash Flows and (iv) provided information about the activities of the Authority, present an image of the Authority finances. These statements show how these services were financed in the short-term as well as what remains for future activities.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

OVERVIEW OF THE FINANCIAL STATEMENTS:

The Authority is a component unit of the Commonwealth of Puerto Rico and is presented in the Commonwealth government wide financial statements as an enterprise fund.

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED):

Government-wide Statements consist of a statement of net assets and statement of activities prepared using the economic resources measurement focus and accrual basis of accounting. These statements will report all the assets, liabilities, revenues and expenses on the government.

Each statement will distinguish and between the governmental and business-type activities of the primary government and between the total primary government and it's discretely presented component units by reporting each in separated columns. Fiduciary activities, whose resources are not available to finance the government's programs, will be excluded from the government-wide statements.

An enterprise fund essentially encompasses the same functions reported as business-type activities in the government-wide statements. Substantially all services are provided to customers not related to the Commonwealth of Puerto Rico.

The Authority's basic financial statements are presented attached to this document and are accompanied by notes to the Basic Financial Statements, which provide information essential to their full understanding.

Statement of Net Assets

The statement of the net Assets presents the Authority's statements of positions as of June 30, 2012, showing information that includes all of the Authority's assets and liabilities, as well as the net assets. Evaluation of the overall financial health of the Authority would extend to external factors such as the quality if the portfolio of investments and related market conditions, and the experience of gains and losses that may be affected by demographic variables, and the inflationary increase of medical costs.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

Statement of revenues, Expenses, and Changes in Net Assets

The statements of revenues, expenses and changes in net assets show how the Authority's net assets changed during the fiscal year. All current fiscal year revenues and expenses are regardless of when cash is received or paid. An important purpose of the design of this statement is to show the financial reliance of the Authority's functions on revenues earned.

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED):

Statement of Cash Flows

The statement of cash flows presents the sources and uses of cash flows divided in four categories: operating activities, non-capital financing activities, capital and related financing activities and investing activities. The statement reconciles net cash and cash equivalents at the beginning and end of year and reconciles the net income (loss) with the cash used in operating activities to provide an explanation of cash and non-cash activities within the statement of revenues, expenses and changes in net assets.

FINANCIAL ANALYSIS OF THE AUTHORITY AS A WHOLE:

The Authority is a public corporation and a governmental instrument of the Commonwealth of Puerto Rico, created by Law No. 70 of June 23, 1978, as amended. The main purpose of the Authority is to provide alternatives for the processing of solid waste in Puerto Rico. Also, in accordance with the law, the Authority has the responsibility of educating the community in this respect as well as the development and implementation of the required programs needed for the reduction and reuse of solid waste.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

Our analysis, as shown below, focuses on net assets (Table 1) and change in net assets (Table 2) for the Authority's activities compared to prior year:

TABLE 1- STATEMENT OF NET ASSETS

	<u>2012</u>	<u>2011</u>	<u>Total % Change</u>
ASSETS			
Current assets	\$ 27,848,691	\$ 27,200,230	2%
Restricted assets	15,172,365	10,847,157	40%
Investment in preferred stock	500,000	500,000	0
Due from Commonwealth of Puerto Rico	673,767	-----	100%
Capital assets-net	<u>138,158,028</u>	<u>138,495,625</u>	<u>-.2%</u>
Total Assets	<u>\$ 182,352,851</u>	<u>\$177,043,012</u>	<u>3%</u>
LIABILITIES			
Current liabilities	\$ 91,061,369	\$ 82,528,585	10%
Long-term debt	<u>12,856,512</u>	<u>14,578,104</u>	<u>-12%</u>
Total current liabilities	<u>103,917,881</u>	<u>97,106,689</u>	<u>7%</u>
Net Assets:			
Investment in capital assets, net of related debt	63,741,623	76,485,838	-17%
Restricted for federal projects	125,738	176,741	-29%
Restricted for state projects	6,000,000	-----	100%
Unrestricted	<u>8,567,609</u>	<u>3,273,744</u>	<u>162%</u>
Total net assets	<u>78,434,970</u>	<u>79,936,323</u>	<u>2%</u>
Total liabilities and net assets	<u>\$ 182,352,851</u>	<u>\$177,043,012</u>	<u>3%</u>

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

As observed from the table above, the Authority's net assets increased from \$77,651,006 to \$84,434,970. The increase in net assets was primarily due to net effect of an increase in revenues arriving from contracts which increased by approximately \$240,344, the depreciation expenses decreased by approximately \$184,211. Also, the Authority experienced a voluntary retirement benefit expenses of approximately \$1,616,737 (which means a reduction of \$2,774,706, compared with the previous year) which arose from the enactment of the Act. No. 70 and the present value of the future benefits payable was accrued as a period expense. The Authority reduced its general and administrative expenses by \$577,054 or -17%, also the economic assistance programs, implemented during the year, obtained an increase of approximately \$1,653,578 or 73%. Total liabilities of the Authority increased by \$4,525,875 million or 5%.

TABLE -2 REVENUES, EXPENSES, AND CHANGE IN NET ASSETS

	<u>2012</u>	<u>2011</u>	<u>Total % Change</u>
Operating Revenues:			
Contract revenues	\$ 1,254,412	\$ 1,014,068	24%
Miscellaneous	11,680	21,844	-47%
	<u>1,266,092</u>	<u>1,035,912</u>	<u>22%</u>
Operating Expenses:			
Depreciation and amortization	6,167,642	6,351,853	-3%
Voluntary termination benefits	1,616,737	4,391,443	-63%
General and administrative	2,906,995	3,484,049	-17%
Salaries and fringe benefits	2,839,026	3,304,068	-14%
Economic assistance programs	3,930,601	2,277,023	73%
Insurance	803,261	522,862	54%
Repairs and maintenance	226,683	179,549	26%
Rent	1,240	4,575	-73%
Land field project	974,353	-----	100%
	<u>19,466,538</u>	<u>20,515,422</u>	<u>-5%</u>
Total operating expense			
Operating loss before non-operating revenues (expenses)	<u>\$ (18,200,446)</u>	<u>\$ (19,479,510)</u>	<u>7%</u>

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

	<u>2012</u>	<u>2011</u>	<u>Total % Change</u>
Non-Operating Revenues (Expenses):			
Interest and dividends income	\$ 202,377	\$ 498,711	-59%
Interest expenses	(5,778,396)	(5,606,848)	-3%
Loss on extinguishment of debt	(25,035)		100%
Gain on sale of equipment	200,500		100%
Capital contributions from the Commonwealth of Puerto Rico	<u>18,197,335</u>	<u>15,079,941</u>	<u>21%</u>
Total non-operating revenues (expenses)	<u>12,796,781</u>	<u>9,971,804</u>	<u>28%</u>
 Change in Net Assets	 (1,501,353)	 (9,507,706)	 84%
Net Assets, beginning of year	79,936,323	87,158,712	-8%
Restatement of net assets		<u>2,285,317</u>	
Net Assets, beginning of year, as restated	<u>79,936,323</u>	<u>89,444,029</u>	<u>-8%</u>
Net Assets, end of year	<u>\$ 78,434,970</u>	<u>\$ 79,936,323</u>	<u>2%</u>

As observed from table 2 in previous page, the Authority's total contract revenues increased by \$240,344 or 24%.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets:

Capital assets consist mostly of land and structures, the majority of which are acquired or constructed to provide alternatives for the collection and processing of solid waste. At the end of fiscal year 2012, Authority had \$138,573,923 invested in a broad range of capital assets (See Table 3). This amount represents a net increase, including additions and deductions, of approximately \$78,298 over the prior year.

SOLID WASTE AUTHORITY
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MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

**TABLE 3- CAPITAL ASSETS, NET
OF ACCUMULATED DEPRECIATION AND AMORTIZATION**

	<u>2012</u>	<u>2011</u>
Land	\$ 12,966,607	\$ 12,966,607
Building, improvement and equipment, net	108,544,082	115,063,234
Construction in progress	<u>16,647,339</u>	<u>10,465,784</u>
Total capital assets	<u>\$ 138,158,028</u>	<u>\$ 138,495,625</u>

TABLE 4- OUTSTANDING DEBTS AT YEAR END

	<u>2012</u>	<u>2011</u>
Current Liabilities		
Accounts payable-trade	\$ 10,217,532	\$ 8,442,195
Current portion:		
Bank credit lines	74,416,405	68,947,628
Accrued compensated absences	291,999	305,333
Accrued expenses	6,131,548	7,032,153
Deferred revenues	<u>3,885</u>	<u>3,885</u>
Total current liabilities	<u>91,061,369</u>	<u>84,731,194</u>
Long-term liabilities:		
Bank credit lines	7,777,895	10,689,497
Accrued compensated absences	371,635	388,607
Accrued expenses	165,865	-
Due to other governmental entities	<u>4,541,117</u>	<u>3,500,000</u>
Total long-term liabilities	<u>12,856,512</u>	<u>14,578,104</u>
Total liabilities	<u>\$ 103,917,881</u>	<u>\$ 99,309,298</u>

Decrease in accrued expense of \$900,605 is due to a decrease in salaries and fringe benefit result commonwealth enacted Law No.70 to establish a program that provides benefits for early

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MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2012

retirement or economic incentives for voluntary employment terminations to eligible employees, as defined, including employees of the Authority.

The Authority is a defendant in various lawsuits. The Authority and its internal and external legal representatives are of the opinion that it is not possible to predict as of the financial statements date the outcome of these lawsuits.

CURRENT AND NEXT YEAR BUDGET

During the fiscal year ending June 30, 2012, an increase in funds to pay the outstanding balances on all credit lines with Government Development Bank of Puerto Rico (GDB) had an impact on the Authority's budget. These credit lines were obtained for the acquisition, prior to June 30, 2008, of build facilities that allowed the centralization of agencies relating to the environment, such as the Solid Waste Authority, the Department of Natural Resources, the Energy Office and the Environmental Quality Board. It also allowed continuing with the development of infrastructure project directly related with the disposition of solid waste in the Commonwealth of Puerto Rico.

For the fiscal year 2012-2013 a consolidated budget of \$6,394,000 was assigned to the Solid Waste Authority.

CONTACTING THE ADMINISTRATION FINANCIAL MANAGEMENT

The financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the Authority's finance and to show the Authority's accountability for the funds it receives. If you have questions about this report or need additional information, contact the Management Affair Director or Finance Director at (787) 765-7575.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
STATEMENT OF NET ASSETS
JUNE 30, 2012

ASSETS

CURRENT ASSETS

Cash and cash equivalents (Notes 2, 3, and 14)	\$ 3,192,803
Investments at fair value (Notes 2 and 4)	18,608,338
Accounts receivable, net of allowance for doubtful accounts of \$2,879,371 (Notes 2, 5, and 14)	5,878,461
Prepaid expenses	200
Restricted funds, cash and cash equivalents (Note 3)	15,172,365
Total current assets	42,852,167

NONCURRENT ASSETS

Other assets	168,889
Due from Commonwealth of Puerto Rico	673,767
Capital assets, net (Notes 2 and 6)	138,158,028
Investment in preferred stocks (Notes 2 and 7)	500,000
Total noncurrent assets	139,500,684
Total assets	\$ 182,352,851

The accompanying notes are an integral part of these financial statements.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
STATEMENT OF NET ASSETS (CONTINUED)
JUNE 30, 2012

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES

Credit lines (Note 10)	\$ 74,416,405
Accounts payable, trade	3,633,608
Accrued compensated absences	291,999
Accrued expenses	6,131,548
Due to other governmental entities (Note 8)	6,583,924
Deferred revenues	3,885
Total current liabilities	91,061,369

NONCURRENT LIABILITIES

Loans payable (Note 11)	7,777,895
Due to other governmental entities (Note 8)	4,541,117
Accrued expenses	165,865
Accrued compensated absences	371,635
Total noncurrent liabilities	12,856,512

Total liabilities	103,917,881
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COMMITMENTS AND CONTINGENCIES (Notes 12 and 13)

NET ASSETS

Investment in capital assets, net of related debt	63,741,623
Restricted for federal projects	125,738
Restricted for state projects	6,000,000
Unrestricted	8,567,609
Total net assets	78,434,970

Total liabilities and net assets	\$ 182,352,851
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The accompanying notes are an integral part of these financial statements.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2012

OPERATING REVENUES	
Contract revenues (Note 2)	\$ 1,254,412
Miscellaneous	11,680
Total operating revenues	<u>1,266,092</u>
OPERATING EXPENSES	
Depreciation and amortization (Notes 2 and 6)	6,167,642
Voluntary termination benefits	1,616,737
General and administrative	2,906,995
Salaries and fringe benefits	2,839,026
Educational campaign	3,930,601
Insurance	803,261
Repairs and maintenance (Note 2)	226,683
Landfill projects	974,353
Rent	1,240
Total operating expenses	<u>19,466,538</u>
OPERATING LOSS BEFORE NON-OPERATING REVENUES (EXPENSES)	<u>(18,200,446)</u>
NON-OPERATING REVENUES (EXPENSES)	
Interest and dividends income (Notes 4 and 7)	202,377
Loss on extinguishment of debt	(25,035)
Gain on sale of equipment	200,500
Interest expense (Notes 10 and 11)	(5,778,396)
Capital contributions from Puerto Rico Sales Tax Financing Corporation (Note 11)	3,902,312
Capital contributions from the Commonwealth of Puerto Rico	18,197,335
Total non-operating revenues (expenses)	<u>16,699,093</u>
CHANGE IN NET ASSETS	<u>(1,501,353)</u>
NET ASSETS AT BEGINNING OF YEAR	77,651,006
RESTATEMENT OF NET ASSETS (Note 16)	<u>2,285,317</u>
NET ASSETS AT BEGINNING OF YEAR, AS RESTATED	<u>79,936,323</u>
NET ASSETS AT END OF YEAR	<u>\$ 78,434,970</u>

The accompanying notes are an integral part of these financial statements.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2012

CASH FLOWS FROM OPERATING ACTIVITIES

Cash received from contracts and others	\$ 890,954	
Cash paid to suppliers	(6,249,347)	
Cash paid for salaries and fringes	(2,869,332)	
Cash received from other sources	11,680	
Net cash used in operating activities	<u>(8,216,045)</u>	

CASH FLOWS PROVIDED BY NON-CAPITAL FINANCING ACTIVITY

Contributions from the Commonwealth of Puerto Rico	16,225,775	
Contribution from Puerto Rico Sales Tax Financing Corporation	3,902,312	
Net cash provided by non-capital financing activities	<u>20,128,087</u>	

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Proceeds from credit line and others	6,331,461	
Purchase of property and equipment, and construction of property	(5,629,545)	
Principal payments on loans	(3,902,312)	
Repayment of credit lines	(862,684)	
Interest paid	(4,672,552)	
Net cash used in capital and related financing activities	<u>(8,735,632)</u>	

CASH FLOWS FROM INVESTING ACTIVITIES

Interest and dividends received	901,806	
Change in value of investments	6,711	
Net cash provided by in investing activities	<u>908,517</u>	

NET INCREASE IN CASH AND CASH EQUIVALENTS

4,084,927 ✓

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR

14,280,241 ✓

CASH AND CASH EQUIVALENTS AT END OF YEAR

\$ 18,365,168 ✓

The accompanying notes are an integral part of these financial statements.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
STATEMENT OF CASH FLOWS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2012

**RECONCILIATION OF OPERATING LOSS TO NET CASH USED
IN OPERATING ACTIVITIES**

Operating loss before non-operating revenues and contributions	<u>\$ (18,200,446)</u>
Adjustments to reconcile operating loss to net cash used in operating activities:	
Depreciation and amortization	6,167,642
Change in assets and liabilities:	
Increase (decrease) in:	
Accounts receivable	(363,458)
Prepaid insurance	144,516
Other assets	5,010
Decrease (increase):	
Accounts payable	1,775,337
Accrued expenses	<u>2,255,354</u>
Total adjustments	<u>9,984,401</u>

NET CASH USED IN OPERATING ACTIVITIES \$ (8,216,045)

**RECONCILIATION OF CASH AND CASH EQUIVALENTS WITH
THE STATEMENT OF NET ASSETS**

Cash in current assets	\$ 3,192,803
Cash restricted	<u>15,172,365</u>
	<u><u>\$ 18,365,168</u></u>

The accompanying notes are an integral part of these financial statements.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEARS ENDED JUNE 30, 2012

1. REPORTING ENTITY

The Solid Waste Authority (the Authority) is a public corporation and a governmental instrumentality of the Commonwealth of Puerto Rico, created by Law No. 70 of June 23, 1978, as amended. The main purpose of the Authority is to provide alternatives for the processing of solid waste in Puerto Rico. Also, in accordance with the law, the Authority has the responsibility of educating the community in this respect as well as the implementation of the required programs needed for the reduction and reuse of solid waste.

Pursuant to the Reorganization Plan Number 1 of 1993, the Authority is under the oversight of the Department of Natural and Environmental Resources of Puerto Rico (the Department). The Secretary of the Department is the President of the Governing Board of the Authority.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Basis of Accounting

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting in conformity with accounting principles generally in the United States of America. Proprietary funds are used to account for business-type activities, which are financed mainly by fees and charges to users for the services provided by the funds operations. Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

b. Basis of Presentation

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

SOLID WASTE AUTHORITY
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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEARS ENDED JUNE 30, 2012

of net assets into three components: invested in capital assets, net of related debt; restricted; and unrestricted, described as follows:

- Invested in capital assets, net of related debt – Consists of capital assets, net of accumulated depreciation reduced by the outstanding balance of any bonds, mortgage, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets. Significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.
- Restricted – This component of net assets consists of constraints placed on net assets use through external constraints imposed by creditors (such as through covenants), contributors, or law or regulations of other governments or constraints imposed by law through constitutional provision or enabling legislation.
- Unrestricted – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

As permitted by GASB Statement No. 20, *“Accounting and Financial Reporting for Proprietary Funds and other Governmental Entities that use Proprietary Fund Accounting”* the Authority has elected to apply all Financial Accounting Standards Board Statements and Interpretations, issued after November 30, 1989 that does not conflict with those issued by GASB.

c. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results may differ from those estimates.

SOLID WASTE AUTHORITY
(A Component Unit of the Commonwealth of Puerto Rico)
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEARS ENDED JUNE 30, 2012

d. Statement of Cash Flows

The Authority prepares its statements of cash flows using the direct method. For the purpose of this statement the Authority includes as cash equivalents all unrestricted and restricted highly liquid debt instruments with original maturities of three months or less at time of purchase.

e. Fair Value of Financial Instruments

The carrying amounts reported in the statement of net assets for cash and cash equivalents and receivables, approximate fair value due to their short-term duration.

f. Non-exchange Transactions

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

g. Contract Revenues

Contract revenues arise from the lease of heavy equipment to different municipalities of Puerto Rico for the collection of solid waste and the operations of landfills, and with other agencies, principally the Department of Natural and Environmental Resources for the collection of debris and vegetative materials.

h. Accounting for Pension Costs

The Authority accounts for pension costs in accordance with the provisions of GASB Statement No. 27, *"Accounting for Pensions by States and Local Governmental Employers"*.

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GASB Statement No. 27 establishes standards of accounting and financial reporting for pension expenditures/expenses and related pension liabilities, pension assets, note disclosures, and required supplementary information in the financial reports of state and local governmental employers. The statement defines that the pension expense is equal to the statutory required contributions to the employees' retirement system. A pension liability or asset is reported equal to the cumulative difference between statutory required and actual contributions.

i. Cash Equivalents

Cash equivalents are defined as highly liquid investments with original maturities at the date of purchase of 90 days or less, excluding resources held in restricted accounts. The Commonwealth requires that public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth.

j. Allowance for Doubtful Accounts

The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible losses on existing receivables, excluding debt service rentals and maintenance charges that may become uncollectible based on evaluations of the collectability of each balance. Because of uncertainties inherent in the estimation process, management's estimate of losses in the receivables outstanding and the related allowance may change in the near term. As of June 30, 2012, the allowance for doubtful accounts for other receivables amounted to \$2,897,371.

k. Investments

The Authority is permitted by law to invest on eligible corporations related to solid waste management. Investments in preferred stocks of such corporations are recorded at acquisition cost, as these are not held for investment purposes or to generate profit or gain on the investments, but rather as an incentive to assist organizations related to waste management.

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Investments in debt instruments have been classified and presented in accordance with GASB Statement No. 31 *"Accounting and Financial Reporting for Certain Investments and for External Investments Pools"*. In accordance with this statement, investments are presented at fair market value in the statement of net assets.

Unrealized holding gains or losses related to the valuation of the investments are presented as an increase or reduction in the Statement of Revenues, Expenses and Change in Net Assets, as part of the current period interest and dividends income. Realized gains and losses for investments are reported in as current earnings or losses in the Statement of Revenues, Expenses and Change in Net Assets based on the adjusted cost of the specific investments sold.

I. Capital Assets

Capital assets, consisting mostly of land and structures, the majority of which are used to provide alternatives for the collection and processing of solid waste, are carried at cost. Donated capital assets are recorded at estimated fair market value at the date of donation. Major renewals and betterments that materially extend the capacity or efficiency or extend the useful life of an asset are capitalized while replacements, maintenance, and repairs which do not improve or extend the life of the respective assets are charged to expense in the period incurred. Upon retirement or other disposal of properties, the related cost and accumulated depreciation and amortization are removed from the accounts. Gains or losses on sales or retirement of properties are reflected in the statement of revenues, expenses, and change in net assets.

The Authority's capital assets are depreciated or amortized over the estimated useful lives of the related assets or the term of the lease agreement, whichever is shorter, using the straight-line method. Construction in progress is carried at cost during the construction stage and is not depreciated until completion of the related project.

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Major classification and related estimated useful lives of the capital assets are summarized as follows:

	Estimated Useful Lives
Building	30 years
Building improvements	30 years
Airplane	12 years
Project equipment	5 to 10 years
Vehicle	5 years
Furniture and fixtures	2 to 5 years

The Authority periodically reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Management evaluated the costs incurred in construction in process and determined various projects to be impaired on prior years, mostly due to stopping of project by executive order 2001-58A. The total impairment amounted to \$25,698,593 which was recorded as a cost of prior year operations and adjusted against the net assets.

m. Compensated Absences

The vacations policy of the Authority generally provides for the accumulation of thirty (30) days of vacation and eighteen (18) days of sick leave annually. Vacation time is fully vested to the employees from the first day of work. In the event of resignation, an employee is reimbursed for accumulated vacations days up to the maximum allowed of sixty (60) days.

Separation of employment prior to the use of all or part of the sick leave terminates all rights for compensation except that, in the event of retirement, an employee is reimbursed for accumulated sick leave days up to the maximum allowed of ninety (90) days. A liability is reported for accrued but unused vacation and sick leave days.

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n. Adoption of Future Accounting Pronouncements

The Governmental Accounting Standards Board has issued the following accounting standards that have effective dates after June 30, 2012 for the Authority:

Statement Number	Statement Name	Adoption Required in Fiscal Year
60	Accounting and Financial Reporting for Service Concession Arrangements	2012-13
61	The Financial Reporting Entity: Omnibus- An amendment of GASB Statements No. 14 and 34	2012-13
62	Codification of Accounting and Financial Reporting Guidance Contained in Pre - November 30, 1989 FASB and AICPA Pronouncements	2012-13
63	Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position	2012-13
65	Items Previously Reported as Assets and Liabilities	2013-14
66	Technical Corrections - 2012- an amendment of GASB Statements No. 10 and 62	2013-14
67	Financial Reporting for Pension Plans - an amendment of GASB Statement No. 25	2013-14
68	Accounting and Financial Reporting for Pensions - and amendment of GASB Statement No. 27	2014-15

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3. CASH AND CASH EQUIVALENTS

As of June 30, 2012, cash unrestricted and restricted include certain cash, cash equivalents, certificates of deposit, money market and others, as follows:

Unrestricted Cash and Equivalents

Cash	\$ 2,634,509
Money Market (investment related)	<u>558,294</u>
Total	<u>\$ 3,192,803</u>

Restricted Cash

Development of infrastructure projects	\$ 9,492,093
Financial assistance	3,657,756
Other programs	<u>2,022,516</u>
Total	<u>\$ 15,172,365</u>

4. INVESTMENTS

The following reflects the amortized cost and estimated fair values of investments held at fair value as of June 30, 2012. In addition, gross unrealized gains and losses are as follow:

	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Gain</u>
Corporate Bonds	\$ 11,811,089	\$ 11,827,394	\$ 16,305
Other Securities	<u>6,054,148</u>	<u>6,780,944</u>	<u>726,796</u>
Total	<u>\$ 17,865,237</u>	<u>\$ 18,608,338</u>	<u>\$ 743,101</u>

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The maturities of investments and their approximate market value as of June 30, 2012, were as follows:

	Cost	Market Value
Within one (1) year or less	\$ 12,406,022	\$ 13,136,094
After one (1) year through five (5) years	5,459,215	5,472,244
Total	\$ 17,865,237	\$ 18,608,338

a. Interest Rate Risk

The Authority maintains investments in debt instruments with the United States Government and Corporate bonds. The market value of such investment instruments varies and is dependable of changes in interest rates. The Authority does have an investment policy that requires an evaluation of the investment portfolio every twelve months as a means of managing its exposure to declines in fair value and losses arising from increasing interest rates, so the investment portfolio manager can take the necessary actions to protect the Authority's investment. Nevertheless, the Authority is exposed to the risk of not recovering the market value of such investments due to fluctuations in interest rates.

b. Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in possession of an outside party. As of June 30, 2012, the Authority's external investments did not have any securities exposed to custodial credit risk and there was no securities lending.

The Authority maintains investment and cash accounts with stock brokerage firms. The Securities Investor Protection Corporation (SIPC) protects, in most cases, securities up to a ceiling of \$500,000 per customer, as long as it is invested in money market funds. For short-term securities it is directly related to their credit rating. Also, it provides protection up to \$100,000 in cash claims. The brokerage firm also maintains private insurance coverage, for custodial purposes only, which exceeds the balance of the investment. As of June 30, 2012, the investment in securities balance exceeds the insured limits but they have been placed in high

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credit standing institutions and management of the Authority believes that custodial credit risk related to these investments and deposits are minimum.

c. Credit Risk

The Authority is exposed to credit risk, since the investment policy do not set forth the minimum acceptable credit ratings from any of the nationally recognized statistical rating organizations, although the policy limits its investment choices for investments to bonds and notes of the Federal Treasury, bonds and notes of Federal and State Agencies, and any other investment that guarantees principal.

d. Concentration of Credit Risk

Although the investment policy limits its investment choices for investments to bonds and notes of the Federal Treasury, bonds and notes of Federal and State Agencies, and any oilier investment that guarantees principal, the Authority places no limit on the amount it may invest in any one issuer of investment instruments.

5. ACCOUNTS RECEIVABLE

As of June 30, 2012, accounts receivable consisted of the following:

Department of Natural Environment Resources	\$ 2,988,536
Other governmental agencies	1,730,492
Municipalities	734,372
Commonwealth of Puerto Rico	1,507,168
Others	1,797,264
	<hr/>
	8,757,832
Allowance for doubtful accounts	<u>(2,879,371)</u>
	<hr/>
Total	<u>\$ 5,878,461</u>

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6. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2012, were as follows:

	<u>Beginning Balance, as restated</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 12,966,607	\$ -	\$ -	\$ 12,966,607
Construction in progress	10,465,784	6,181,555		16,647,339
Total capital assets, not being depreciated	<u>23,432,391</u>	<u>6,181,555</u>	<u>-</u>	<u>29,613,946</u>
Capital assets, being depreciated:				
Buildings	93,979,993			93,979,993
Mini transfer stations	42,131,063			42,131,063
Project equipment	15,875,565			15,875,565
Building improvements	14,993,998			14,993,998
Office furniture	7,361,352	21,299	(15,000)	7,367,651
Motor vehicles	1,221,930		(372,800)	849,130
Airplanes	461,000		(461,000)	-
Leasehold improvements	262,629			262,629
	<u>176,287,530</u>	<u>21,299</u>	<u>(848,800)</u>	<u>175,460,029</u>
Less accumulated depreciation for:				
Buildings	(20,695,055)	(3,132,610)		(23,827,665)
Mini transfer stations	(14,539,837)	(1,404,367)		(15,944,204)
Project equipment	(15,191,836)	(195,596)		(15,387,432)
Building improvements	(2,894,746)	(499,799)		(3,394,545)
Office furniture	(6,359,771)	(905,577)	15,000	(7,250,348)
Motor vehicles	(819,431)	(29,693)		(849,124)
Airplanes	(461,000)		461,000	-
Leasehold improvements	(262,629)			(262,629)
	<u>(61,224,305)</u>	<u>(6,167,642)</u>	<u>476,000</u>	<u>(66,915,947)</u>
Total capital assets, being depreciated, net	<u>115,063,225</u>	<u>(6,146,343)</u>	<u>(372,800)</u>	<u>108,544,082</u>
Capital assets, net	<u>\$ 138,495,616</u>	<u>\$ 35,212</u>	<u>\$ (372,800)</u>	<u>\$ 138,158,028</u>

7. INVESTMENT IN PREFERRED STOCKS

The Authority is allowed by its laws and regulations to invest directly in eligible corporations that are related with the collection, disposition, construction or operations of solid waste facilities. The eligible corporation must be established or must be authorized to do business in Puerto Rico and must exercise a role in the management of the solid waste and/or recycling infrastructure. The operations of the corporation must be in accordance with the Regional Plan for Disposition and Recycling of the

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Solid Waste of Puerto Rico and/or the Plan for Reduction, Reuse and Recycling for Puerto Rico.

As of June 30, 2012, the Authority has invested in two (2) eligible corporations dedicated to the recycling of plastic and battery waste and to the development and commercialization of anaerobic technology for the treatment of poultry wastes. The Authority also invested in other three (3) eligible corporations; Safetech Corporation, Novo Recicladores, Inc., and Biorganic Energy, Inc. The value of the preferred stocks from those corporations was reduced to zero. The equity securities are all held by the Authority. The market value of the preferred shares is not available as of June 30, 2012.

The following summarizes the cost, preferences, special rights and restrictions of the preferred shares as of June 30, 2012, as set forth in the stock purchase agreements among the Authority and the investees:

<u>Investee</u>	<u>Description</u>	
The Battery Recycling Co., Inc.	200 shares of Class A, convertible preferred stock with a par value of \$1,000 per share. The preferred stockholder will receive a preferred cumulative dividend of 6% per annum payable quarterly.	\$ 200,000
Grupo Comunitario de Reciclaje, Inc. P.T.	3,000 shares of Class A preferred stock with a par value of \$100 per share. The preferred stockholder will receive a dividend that will vary from 0% to 15% through the five (5) years period that cover the stock purchase agreement.	<u>300,000</u>
		<u>\$ 500,000</u>

The shares of preferred stock have liquidation preferences, conversion, anti-dilutive clauses, pre-emptive rights, representation in the Board of Directors of the corporations and certain redemption provisions.

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8. DUE TO OTHER GOVERNMENTAL ENTITIES

Due to other governmental agencies as of June 30, 2012, were as follows:

Puerto Rico Electric Power Authority	\$ 5,284,453
Puerto Rico Aqueduct Sewer Authority	989,134
Natural Resources Department	217,165
Employee Retirement System	33,420
Puerto Rico Labor Department	31,546
Puerto Rico Treasury Department	<u>28,206</u>

Due to other governmental entities - current portion \$ 6,583,924

State Insurance Fund Corporation \$ 4,541,117

Due to other governmental entities - long-term portion \$ 4,541,117

9. PENSION PLAN

The Employees' Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (ERS) is a cost-sharing multiple-employer defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Authority under age fifty five (55) at the date of employment become members of the ERS as a condition to their employment.

The ERS provides retirement; death and disability benefits pursuant to Act 447 approved on May 15, 1951, as amended, and became effective on January 1, 1952. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten (10) years of plan participation.

Members who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained age of at least fifty-eight (58) years and have completed at least ten (10) years of creditable service, are entitled to annual benefits, payable monthly for life. The amount of the annuity shall be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty

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of years of creditable service in excess of twenty years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least thirty years (30) of creditable service are entitled to receive the Merit Annuity. Participants who have not attained fifty-five (55) years of age will receive sixty five percent (65%) of the average compensation or if they have attained fifty-five (55) years of age will receive seventy five percent (75%) of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of service. No benefit is payable if the participant receives a refund of his accumulated contributions.

The legislation of the Commonwealth of Puerto Rico requires employees to contribute 5.775% for the first \$6,600 of their annual gross salary and 8.275% for the salary in excess of \$6,600 for employees hired on or before March 31, 1990. For employees hired on or after April 1, 1990, the required contribution is 8.275% of the gross salary. The Authority's contribution is 10.275% of the gross salary.

Total employee and employer's contributions during the year ended June 30, 2012 amounted to approximately \$168,000. Total payroll covered for the year was approximately \$1.6 million.

On September 24, 1999, an amendment to Act. No. 447 of May 15, 1952, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employees participating in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Authority on or after January 1, 2000, will only be allowed to become members of System 2000. System 2000 reduced the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990. System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan there is a pool of pension assets which are invested by System 2000, together with those of the current defined benefit plan. Benefits at retirement age are not guaranteed by the Commonwealth of Puerto Rico.

The annuity is based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note, or (2) earn a rate equal to seventy-five percent (75%) of the return of the ERS's investment portfolio (net of management

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fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not granted under System 2000. The employee's contribution (10.275% of the employee's salary) is used to fund the current plan.

Additional information on ERS is provided in its financial statements for the year ended June 30, 2012, a copy of which can be obtained by writing to the System's administrator at 437 Ponce de León Avenue, Hato Rey, Puerto Rico 00918.

10. CREDIT LINES

On January 4, 2000, the Authority entered into a loan agreement (the Note) with the Government Development Bank for Puerto Rico for a non-revolving line-of-credit in an amount not to exceed \$112,000,000 for the development of an infrastructure project. Infrastructure project costs incurred are disbursed by the Bank to the Authority. The interest, based on the lender's cost of funding for tax exempt variable rate loan transactions or the cost of any similar obligations to fund the loan is payable quarterly. The credit line was due originally and payable on June 30, 2006. On December 4, 2007, the availability of the credit line was extended to June 30, 2009. On November 23, 2009 was extended to June 30, 2018. Per approved budget for fiscal year 2001-2002 of the Commonwealth of Puerto Rico, as submitted by the Office of Management and Budget, \$25,000,000 have been used for amortizing this bank's credit line.

The credit line was to be paid in four (4) annual installments of \$25,000,000 and the remaining final balance during the next sixth (6) years. The outstanding balance at June 30, 2012 amounted to \$28,229,276.

On May 5, 2003, the Authority entered into a loan agreement related to another non-revolving line-of-credit in an amount not to exceed \$75,000,000 with the Government Development Bank for Puerto Rico for the acquisition of building facilities (See Note 6). The credit line carries interest based on quarterly variable LIBOR rate plus 1.25% with a minimum annual interest rate of five percent (5%). On June 26, 2008, the availability of the credit line was extended to June 30, 2011. To temper the terms and conditions of the line of credit to economic facts of the Puerto Rico Commonwealth on January 29, 2010 extends the availability to June 30, 2018. The outstanding balance at June 30, 2012 amounted to \$46,187,129.

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Credit lines activity for the year ended June 30, 2012, was as follows:

Non-revolving credit line of \$112,000,000:	
Balance at beginning of year	\$ 22,218,967
Additions	6,331,461
Payments	<u>(321,152)</u>
Balance at end of year	<u>\$ 28,229,276</u>
Non-revolving credit line of \$75,000,000:	
Balance, beginning of year	\$ 46,728,661
Payments	<u>(541,532)</u>
Balance at end of year	<u>\$ 46,187,129</u>

11. LOANS PAYABLE

During the year ended June 30, 2012, the Puerto Rico Public Finance Corp. (PFC) refinanced the debt of the Authority. The aggregate debt service requirements of the notes will be funded with annual appropriations from the Commonwealth of Puerto Rico.

The outstanding balance of the loan at June 30, 2012 was \$7,777,895 and matures on June 30, 2031. Interest on the unpaid principal amount of the loan is equal to the applicable percentage of the aggregate interest payable on the Public Finance Corporation Bonds. Applicable percentage is the percentage representing the proportion of the amount paid by the Public Finance Corporation of the PFC Bonds serviced by the loan to the aggregate amount paid by the Public Finance Corporation on all PFC Bonds issued by the Public Finance Corporation. This loan will be paid from legislative appropriations.

In addition, during the year ended June 30, 2012, the Puerto Rico Sales Tax Financing Corporation contributed approximately \$3.9 million for the payment of principal and interests due on such loan payable. Such transactions have been reflected as a contribution from the Puerto Rico Sales Tax Financing Corporation in the accompanying statement of Revenues, Expenses and Changes in Net Assets.

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Aggregate maturities and interest payments of the loan, are as follows:

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Interest</u>
2013	\$ -	\$ 452,204	\$ 452,204
2014	-	434,626	434,626
2015	-	434,626	434,626
2016	228,958	425,711	654,669
2017	185,735	422,188	607,923
2018-2022	1,039,983	1,990,075	3,030,058
2023-2027	1,059,320	1,745,749	2,805,069
2028-2032	5,263,899	474,037	5,737,936
Total	<u>\$ 7,777,895</u>	<u>\$ 6,379,216</u>	<u>\$ 14,157,111</u>

Balance at beginning of year	\$ 10,689,497
Payments	<u>(2,911,602)</u>
Balance at end of year	<u>\$ 7,777,895</u>

12. CONTINGENCIES

b. Litigations

The Authority is a defendant in lawsuits arising in the normal course of operations, principally from claims for contract cancellations. According to the laws of the Commonwealth of Puerto Rico, the Authority is fully represented by the Puerto Rico Department of Justice in defense of all legal cases against the Authority. Any claims with negative financial impact would be paid from the resources of the Authority and the Commonwealth of Puerto Rico.

b. Comptroller's Office of Puerto Rico

This entity has issued several reports on audits over the operations of the Authority. The oversight entities, such as the Puerto Rico Department of Justice, are evaluating actions to be taken against the Authority and its employees.

The financial impact, if any, of the possible actions to be taken by the oversight entities cannot be presently determined.

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c. Environmental Concern

The Authority's operations include activities which are subject to state and federal environmental regulations. The Authority is currently involved in the implementation and development of the Infrastructure Regional Plan for Recycling and Disposal of Solid Waste in Puerto Rico. As of June 30, 2012, management of the Authority believes that, at this time, there is no sufficient information available to determine the potential amount of related losses, if any, and no provision for losses has been made in the accompanying financial statements. Nevertheless, preventive infrastructure has been constructed to minimize any possible impact or events that occur. In addition, operational plans have been developed to incorporate good maintenance practices.

d. Closure and Post-closure Care Costs

The Authority administers a tract of land in the Municipality of Lajas, Puerto Rico, to deposit acceptable sludge. The Commonwealth of Puerto Rico and federal laws and regulations require certain procedures when the tract of land stops accepting waste and to perform certain maintenance and monitoring functions at the site after closure. Subsequent to June 30, 2007, the Authority commenced the closing of this tract of land. The Authority's management has estimated the obligation for closure and post-closure care costs at \$80,000, based on the nature of the waste being deposited. However, as of June 30, 2012, management of the Authority believes that, at this time, there is no sufficient information available to determine the potential amount of related losses, if any, and no provision for losses has been made in the accompanying financial statements. Also, no studies have been performed by outside independent sources to evaluate the amount estimated and it changes are currently needed in the cost estimated by management for the closing of this tract of land facility.

e. Federal Grants

During the normal course of its operations, the Authority sometimes receives grants from the Environmental Quality Board and the Federal Emergency Management Agency. The grant programs are subject to audit by agents of the granting authorities, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement which may arise as a result of the audits is not considered by management to have a significant effect in the accompanying financial statements.

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13. COMMITMENTS

a. Strategic Plan for Recycling

The Authority initiated in years prior to the year ended June 30, 2012, the implementation and development of the Strategic Plan for Recycling and Disposal of Solid Waste in Puerto Rico at an estimated cost of approximately \$112 million. The first stage consists of the construction of thirty-nine (39) projects to be financed through an interim financing agreement with the Government Development Bank for Puerto Rico (See Note 10). The credit lines under the agreement were paid by the Treasury Department through joint resolutions approved by the Legislature of Puerto Rico. The Authority has continued with the planning and construction of the projects.

b. Dynamic Itinerary for Infrastructure Projects

During May 2008, the Authority approved the "Dynamic Itinerary for Infrastructure Projects of Solid Waste in Puerto Rico". This itinerary defines the strategies for safe and efficient handling of solid waste in Puerto Rico for the next twenty-five (25) years in compliance with all applicable regulations. The Authority proposes this itinerary for the purpose of adopting this plan as the official instrument to guide public policy for the development of infrastructure projects for handling and final disposition of solid waste in Puerto Rico. The projects proposed in the itinerary includes programs to develop facilities for the recovery of recyclable materials (MRP's), facilities for the deposit of acceptable sludge, facilities to convert solid waste to energy, transshipment facilities and lateral expansions to sanitary stuffing systems (SRS). The development of those projects takes into consideration the closing of various SRS. The construction investment is estimated in approximately \$1.9 billion. The Authority projects that financing for these projects will come from both the public and private sectors.

14. CONCENTRATION CREDIT RISK

a. Cash and Cash Equivalents

As of June 30, 2012, the Authority had all of its cash deposited with GDB for \$18,723,822 which are unsecured and uncollaterized. The deposits bear interest at 1.76% per annum.

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b. Accounts Receivable

The accounts receivable balance as of June 30, 2012 is mainly from several municipalities and governmental agencies of Puerto Rico. Nevertheless, management of the Authority considers that concentration to credit risks related to these receivables are minimal because, although the Authority generally does not require collateral and credit losses are provided currently through an allowance for doubtful accounts, they will be collected according to their terms.

15. VOLUNTARY 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 Authority. Act No. 70 established 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' salary, as defined. In this early retirement benefit program, the Authority will make the employer contributions to the Retirement System and pay the corresponding pension until the employee complies with the requirements of age and 30 years of credited service in the Retirement System. Economic incentives are available to eligible employees who have less than 15 years of credited service in the Retirement System or who have at least 30 years of credited service in the Retirement System 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. Additionally, eligible employees that choose to participate in the early retirement benefit program or that choose the economic incentive and have less than 15 years of credited service in the Retirement System are eligible to receive health plan coverage for up to 12 months in a health plan selected by management of the Authority.

The financial impact resulting for the benefits granted to participants on this program was the recognition within the Authority's financial statements of a liability of \$5,747,665 in the statement of net assets as of June 30, 2012 and a charge of \$1,616,737 in the statement of activities for the year ended June 30, 2012. At June 30, 2012, unpaid long-term benefits granted on this program were discounted at 3.34%.

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16. PRIOR PERIOD ADJUSTMENT

During the year ended June 30, 2012, the Authority identified certain accounting errors belonging to prior years. The effect of these adjustments on the Authority's net assets as of June 30, 2011, is as follows

Net assets, beginning of year	\$77,651,006
Restatement adjustment, net:	
Accrued expenses	<u>2,285,317</u>
Net assets, beginning of year, as restated	<u>\$79,936,323</u>

17. SUBSEQUENT EVENTS

Subsequent events have been evaluated through March 6, 2013, which is the date the financial statements were available to be issued for events requiring recording or disclosure in the financial statements for the year ended June 30, 2012.

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COMBINING STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEAR ENDED JUNE 30, 2012

	<u>Administration</u>	<u>Federal Projects</u>	<u>Infrastructure Projects</u>	<u>Total</u>
OPERATING REVENUES:				
Contract revenues	\$ 1,254,412	-	-	\$ 1,254,412
Miscellaneous	-	8,429	3,251	11,680
	<u>1,254,412</u>	<u>8,429</u>	<u>3,251</u>	<u>1,266,092</u>
OPERATING EXPENSES:				
Depreciation and amortization	4,550,080			6,167,642
Voluntary termination benefits	1,616,737	2,639	1,614,923	1,616,737
General and administrative	2,906,995			2,906,995
Salaries and fringe benefits	2,839,026			2,839,026
Educational campaign	3,930,601			3,930,601
Insurance	803,261			803,261
Repairs and maintenance	226,683			226,683
Landfill projects	974,353			974,353
Rent	1,240			1,240
	<u>17,848,976</u>	<u>2,639</u>	<u>1,614,923</u>	<u>19,466,538</u>
OPERATING INCOME (LOSS)	(16,594,564)	5,790	(1,611,672)	(18,200,446)
NON-OPERATING REVENUES (EXPENSES):				
Interest income	202,377			202,377
Loss on extinguishment of debt	(25,035)			(25,035)
Gain on sale of equipment	200,500			200,500
Interest expense	(4,009,456)		(1,768,940)	(5,778,396)
Capital contributions from Puerto Rico Sales Tax Financing Corporation	3,902,312			3,902,312
Capital contributions from the Commonwealth of Puerto Rico	18,197,335			18,197,335
	<u>18,468,033</u>	<u>-</u>	<u>(1,768,940)</u>	<u>16,699,093</u>
CHANGE IN NET ASSETS	\$ 1,873,469	\$ 5,790	\$ (3,380,612)	\$ (1,501,353)

The accompanying notes are an integral part of these financial statements.