Puerto Rico Health Insurance Administration
(A Component Unit of the Commonwealth of Puerto Rico)
Financial Statements
Fiscal Year Ended June 30, 2019

TABLE OF CONTENTS

Aquino, De Córdova, Alfaro & Co., LLP
CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS ADVISORS

Jorge Aquino Barreto, CPA, CVA
Jerry De Córdova, CPA, ESQ
Eduardo González-Green, CPA, CFF, CFE

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Puerto Rico Health Insurance Administration
San Juan, Puerto Rico

Report on the Financial Statements

We have audited the accompanying financial statements of the *Puerto Rico Health Insurance Administration* (the Administration), a component unit of the Commonwealth of Puerto Rico (the Commonwealth), as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Administration's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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 from material misstatement.

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

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

P.O. Box 70262, San Juan, Puerto Rico 00936-8262 • Cecilia's Place Suite C-1, #7 Rosa Street
Isla Verde, P.R. 00979 • Phone (787) 253-9595 • Fax (787) 253-9511

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the *Puerto Rico Health Insurance Administration* as of June 30, 2019, and the respective changes in financial position and its cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in note 13 to the basic financial statements, the financial statements as of June 30, 2019 and for the year then ended have been restated to account for amounts related to GASB Statement No. 73. Our opinion is not modified with respect to this matter.

As discussed in note 1 to the basic financial statements, the Administration is a component unit of the Commonwealth. As of June 30, 2019, the financial condition and liquidity of the Commonwealth is deteriorated. Considering that the Administration depends significantly on appropriations from the Commonwealth, the financial condition and liquidity of the Administration could be similarly affected. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information Omitted

The Administration has omitted the schedules and ratios required by Statement No. 73 of the Governmental Accounting Standards Board, information that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Restatement

In our report dated September 8, 2020 we expressed a qualified opinion on the June 30, 2019 financial statements because the same were not in compliance with GASB Statement No. 73. As described in note 13, the Administration has complied with GASB Statement No. 73 and has restated its June 30, 2019 financial statements to conform with accounting principles generally accepted in the United States of America. Accordingly, our present opinion on the restated June 30, 2019 financial statements as presented herein, is different from that expressed in our previous report.

Carolina, Puerto Rico
September 8, 2020
Except for Note 13 as to which the
date is September 10, 2021

Aquino, De Cordova, Alfaro & Co. LLP

Stamp number E466466
of Puerto Rico CPA Society
has been affixed to the
original report

This section of the financial statements is classified by the Governmental Accounting Standards Board (GASB) as required supplementary information. Management of the Puerto Rico Health Insurance Administration (the Administration or PRHIA) provides this Management Discussion and Analysis for the benefit of readers of the Administration's financial statements. Along with the financial statements and related notes, management's discussion and analysis should provide the most relevant information regarding the financial condition of the Administration for the fiscal year ended June 30, 2019.

Overview of the Financial Statements

This report includes the management's discussion and analysis, the independent auditor's report, and the basic financial statements and related Notes to the Financial Statements. The management's discussion and analysis focus on major components of the financial statements. The financial statements are designed to provide users with a broad overview of the Administration's finance with the intention to help answer the question whether the Administration is better off or worse off financially as a result of this year's activities. These financial statements are prepared under the accrual basis of accounting.

The Statement of Net Position presents information of the Administration's assets, liabilities, and deferred inflows/outflows of resources with the difference reported as net position. Over time, increases or decreases in net position, along with other financial information, serve as a useful indicator of the Administration's financial position and whether it is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Position presents information showing how the Administration's net position changed during the fiscal year ended June 30, 2019. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the cash flows. Therefore, revenues and expenses are reported in this statement for certain items that will result in cash flows in future fiscal periods.

The Statement of Cash Flows shows how the Administration's cash and cash equivalents increased or decreased during the fiscal year reported. It also shows how cash and cash equivalents were provided by and used in the Administration's operating, non-operating and financing, and investing activities. The net increase or decrease in the Administration's cash and cash equivalents is added to the balance at the beginning of year to arrive at cash and cash equivalents balance at end of year. This statement is presented on a cash basis and only presents cash receipts and cash disbursements information. The Administration uses the direct method of presenting cash flows, which includes a reconciliation of operating income to net cash provided by operating activities.

The notes to the financial statements provide additional information that is essential for a thorough understanding of the financial data presented in the financial statements.

These statements and information represent the actual financial condition of the Administration. Following, you will find a condensed discussion of these statements and notes.

Financial Highlights

For the fiscal year ended June 30, 2019, the Administration reported a net position of approximately $202 million, from $202.1 million in prior year. The decrease in net position was primarily driven by the non-contributions from the municipalities.

The condensed Statements of Net Position of the Administration at June 30, 2019 and 2018 were:

	June 30, 2019 As restated	June 30, 2018 As restated	Change In dollars	Change Percentage
Current assets	$ 706,185,595	$ 633,026,217	$ 73,159,378	12%
Non-current assets	14,492,398	20,461,959	(5,969,561)	-29%
Deferred outflows related to pension plan	724,754	3,191,022	(2,466,268)	0%
Total assets and deferred outflows of resources	$ 721,402,747	$ 656,679,198	$ 64,723,549	10%
Current liabilities	$ 378,133,898	$ 285,991,107	$ 92,142,791	32%
Non-current liabilities	140,949,694	165,956,226	(25,006,532)	-15%
Deferred inflows related to pension plan	349,818	2,569,558	(2,219,740)	0%
Total liabilities and deferred inflows of resources	$ 519,433,410	$ 454,516,891	$ 64,916,519	14%
Net position:				
Net investment in capital assets	$ 1,369,791	$ 2,378,174	$ (1,008,383)	-42%
Unrestricted	200,599,546	199,784,133	815,413	0%
Total net position	$ 201,969,337	$ 202,162,307	$ (192,970)	0%
Total liabilities, deferred inflows of resources and net position	$ 721,402,747	$ 656,679,198	$ 64,723,549	10%

As of June 30, 2019, the Administration reported total assets and deferred outflows of resources of approximately $721.4 million, an increase of $64.7 million from prior year. Increase in total assets was mainly due to unexpended cash. For the same period, total liabilities and deferred inflows of resources were $519.4 million, an increase of $64.9million from prior year. Increase in total liabilities was primarily due to increase in premiums and claims payable.

The Administration's net investment in capital assets as of June 30, 2019 amounted to $1,369,791, net of accumulated depreciation. Capital assets include equipment, furniture, leasehold improvements, and vehicles. During the fiscal year ended June 30, 2019, the Administration invested approximately $14,000 and $874,000 in capital assets, respectively. Depreciation and amortization expense for the year ended June 30, 2019 amounted to $1,022,764.

The condensed Statement of Revenues, Expenses and Changes in Net Position for the fiscal year ended June 30, 2019 is as follows:

	June 30, 2019 As restated	June 30, 2018 As restated	Change In dollars	Change Percentage
Operating revenues:				
Contributions from:				
Puerto Rico Department of Health	$ 2,547,711,428	$ 2,177,047,045	$ 370,664,383	17%
Commonwealth of Puerto Rico	14,886,000	556,041,667	(541,155,667)	-97%
Municipalities	-	161,615,820	(161,615,820)	-100%
Employers	29,188,217	28,043,251	1,144,966	4%
Pharmacy rebate program-net	253,607,607	225,487,701	28,119,906	12%
Bad debts expense	(3,490,677)	(38,488,308)	34,997,631	-91%
	2,841,902,575	3,109,747,176	(267,844,601)	-9%
Operating expenses:				
Medical premiums and claims	2,796,145,815	2,858,306,266	(62,160,451)	-2%
General and administrative	38,119,246	37,557,216	562,030	1%
Depreciation and amortization	1,022,764	777,761	245,003	32%
Total operating expenses	2,835,287,825	2,896,641,243	(61,353,418)	-2%
Non-operating revenues, net of expenses:	(6,807,720)	(3,652,837)	(3,154,883)	86%
Change in net position	(192,970)	209,453,096	(209,646,066)	-100%
Net position (deficit), beginning of year	202,162,307	(7,290,789)	209,453,096	2873%
Net position, end of year	$ 201,969,337	$ 202,162,307	$ (192,970)	0%

For the year ended June 30, 2019, the Administration reported operating revenues of approximately $2.8 billion, a decrease of approximately $267.8 million from prior year. The decrease was mainly due to non-contributions from the municipalities and the decrease in contributions from the Commonwealth. Operating expenses were approximately $2.8 billion, a decrease of approximately $61 million. The decrease in operating expenses was mainly as a result of the decrease of medical premiums and claims expense. Non-operating revenues had a combined decrease of approximately $3.2 million primarily due to a decrease in legislative appropriations.

Administration Overview

The Puerto Rico Health Insurance Administration is a public corporation of the Commonwealth of Puerto Rico, created by Act No. 72 on September 7, 1993, as amended. The Administration began operations on February 1, 1994 and is responsible for implementing, administering and negotiating a health insurance program, through contracts with health insurers, mental behavioral health organizations, pharmacy benefit managers, third party administrators and Medicare Advantage organizations, among others. The purpose of the Administration is to provide access to quality medical and hospital care to eligible Puerto Rico residents.

The Administration is the sub-grantee of federal funds provided by the Medicaid Program under Title XIX of the Social Security Act and Title XXI of the State Children's Health Insurance Program (CHIP). The Single State Medicaid Agency is the Puerto Rico Department of Health (the Department of Health).

The Medicaid Program is responsible for administering to the Government Health Insurance Program of federal (those federally eligible for Medicaid) and Commonwealth beneficiaries (those non-eligible for federal Medicaid but who fall within the criteria set forth by Government of Puerto Rico for inclusion within the Government Health Insurance Program).

The Administration and the Medicaid Program have a Memorandum of Understanding in which Medicaid Program delegates full responsibility to the Administration for implementing and administering the Government Health Insurance Program. Among the responsibilities, the Administration is responsible for establishing health coverage for qualified Puerto Rico residents in accordance with the Puerto Rico Medicaid State Plan and negotiating with health insurance organizations for the provision of such covered services, among other.

The executive offices of the Administration are located at 1571 Alda Street, Urb. Caribe, Rio Piedras, Puerto Rico 00926-2712. The Administration's telephone number is (787) 474-3300. Mr. Jorge Galva, Esq. is the Executive Director of the Administration.

Background of Past and Current Healthcare Models

On October 1, 2010, the Commonwealth implemented "Mi Salud" plan, which replaced the "Health Reform" program.

On October 14, 2014, the Board of Directors of the PRHIA awarded new contracts for the GHP, which replaced the former "Mi Salud" plan, to five private insurance providers pursuant to a bidding process. The new contracts became effective on April 1, 2015. Under the new contracts, the Commonwealth public health insurance model changed from a Third-Party Administrator (TPA) model, in which the Commonwealth was ultimately responsible for the cost of the health services provided, to a managed care organization (MCO) model, in which the Administration will pay the MCOs a fixed Per Member Per Month (PMPM) premium for each insured beneficiary and the insurers will be responsible for the cost of such services.

On January 3, 2018, the United States Congress enacted the Bipartisan Budget Act of 2018 and its Act's Division – Supplemental Appropriations, Tax Relief, and Medicaid Changes Relating to Certain Disasters and Further Extension of Continuing Appropriations, (collectively, the "Act"), that was signed into law by President Donald Trump on February 9, 2018. The passage of the Act, through its Titles III, section 20301, Hurricane Maria Relief for Puerto Rico and the Virgin Islands Medicaid Programs, has resulted in health care expanded funding by providing increased caps for the period beginning January 1, 2018, and ending September 30, 2019. The amount of the increase for Puerto Rico was $3.6 billion.

The Act also included a further increase of $1.2 billion if the Secretary certifies that Puerto Rico has taken reasonable appropriate steps during such period, in accordance with a timeline established by the U.S. Secretary of Health (Secretary) to implement methods, satisfactory to the Secretary, for the collection and reporting of reliable data to the Transformed Medicaid Statistical Information System (or a successor system); and demonstrate progress in establishing a State Medicaid Fraud Control Unit (MFCU) as described in section 1903(q).

The changes by the Act established that notwithstanding any other provision of title XIX, during the period in which the additional funds provided are available for Puerto Rico, with respect to payments from such additional funds for amounts expended by Puerto Rico, the Secretary shall increase the Federal Medicaid Assistance Program reimbursable share to 100 percent.

Long-Term Debt

The Administration entered into a Credit Agreement with the Government Development Bank for Puerto Rico on March 14, 2011 in order to pay its obligations to healthcare insurers incurred prior to fiscal year 2009-2010. The aggregate principal amount of the non-revolving line of credit was $186,000,000 and is payable in nine payments of $20,666,667 from 2015 through 2023. Interests are accrued at a fluctuating annual rate of interest equal to the greater of (i) 1.5% over prime rate, and (ii) 6%.

As of June 30, 2019, the accrued interest amounted to $52,698,420. The Administration will pay the principal and interest with appropriations to be received from the Legislature of Puerto Rico through the Puerto Rico Office of Management and Budget (OMB) pursuant to Act No. 173 of 2010. Notwithstanding during the fiscal years ended June 30, 2019, 2018, 2017 and 2016, the OMB failed to make principal and interest payments on behalf of the Administration.

Currently Known Facts

Financial Deterioration of the Commonwealth of Puerto Rico

As disclosed in Note 1, the Administration relies significantly on appropriations from the Commonwealth as well as recurring and non-recurring federal funding. Although the financial condition and liquidity of the Commonwealth has deteriorated, the Administration's has reflected a deficit reduction and surplus due to management cost reductions implementations and improvements on payment eligibility process. Because of the MCO Model Plan, the Administration must focus on the efficiency of the payment eligibility process, for example, adjustments to avoid double payments and deceased members. Furthermore, the Administration works with Cost of Benefit (COB) concept to improve reporting collecting data and reconciliation providing a better future Per Member Per Month (PMPM) payments negotiations.

Subsequent Event

In July 2019, the Administration's ex Executive Director, Mrs. Angela Avila, was arrested and charged with conspiring to favor a consulting firm in obtaining contracts with the Administration.

<u>Contacting the Administration Financial Management</u>

This financial report is designed to provide our customers and creditors with a general overview of the Administration's finances and to demonstrate the Administration's accountability for the federal and commonwealth, among others, funds it receives. If you have questions about this report or need additional information, contact the Puerto Rico Health Insurance Administration, PO Box 195661, San Juan, PR 00926-2706.

* * * * *

Puerto Rico Health Insurance Administration
(A Component Unit of the Commonwealth of Puerto Rico)
Statement of Net Position
June 30, 2019

ASSETS

		2019 As restated
Current assets:		
Cash and cash equivalents	$	283,439,484
Accounts receivable:		
Puerto Rico Department of Health		347,409,848
Pharmacy rebates program		75,262,242
Advance premium		74,021
Total current assets		706,185,595
Non-current assets:		
Accounts receivable:		
Municipalities – net of allowance for doubtful accounts of $89,156,413		-
Legislature appropriations and other – net of allowance for doubtful accounts of $744,520		11,806,407
Due from employers – net of allowance for doubtful accounts of $107,390,496		249,034
Other receivables		414,920
Capital assets – net		1,369,791
Due from MCO's – net of allowance of $10,585,358		652,246
Total non-current assets		14,492,398
Total assets		720,677,993
Deferred outflows of resources:		
Deferred outflows related to pension plan		724,754
Total assets and deferred outflows of resources	$	721,402,747

See accompanying notes to financial statements.

Puerto Rico Health Insurance Administration
(A Component Unit of the Commonwealth of Puerto Rico)
Statement of Net Position - Continued
June 30, 2019

LIABILITIES AND NET POSITION

	2019 As restated
Current liabilities:	
Premiums and claims payable	$ 176,312,567
TPA administration fees payable	80,742,000
Obligation payable Governmental Development Bank	103,333,335
Accounts payable and accrued expenses	15,982,979
Accrued termination benefits	839,045
Accrued compensated absences	923,972
Total current liabilities	378,133,898
Non-current liabilities:	
Obligation payable Governmental Development Bank	79,917,963
Interest payable	52,698,420
Accrued compensated absences	2,783,932
Total pension liability	5,549,379
Total non-current liabilities	140,949,694
Total liabilities	519,083,592
Deferred inflows of resources:	
Deferred inflows related to pension plan	349,818
Total liabilities and deferred inflows of resources	519,433,410
Net position:	
Net investment in capital assets	1,369,791
Unrestricted	200,599,546
Total net position	201,969,337
Total liabilities, deferred inflows of resources and net position	$ 721,402,747

See accompanying notes to financial statements.

Puerto Rico Health Insurance Administration

(A Component Unit of the Commonwealth of Puerto Rico)

Statement of Revenues, Expenses and Changes in Net Position

Fiscal Year ended June 30, 2019

	2019 As restated
Operating revenues:	
Contributions from:	
Puerto Rico Department of Health	$ 2,547,711,428
Commonwealth of Puerto Rico	14,886,000
Municipalities	-
Employers	29,188,217
Pharmacy rebate program – net	253,607,607
Bad debts expense	(3,490,677)
Total operating revenues	2,841,902,575
Operating expenses:	
Medical premiums and claims	2,796,145,815
General and administrative	38,119,246
Depreciation	1,022,764
Total operating expenses	2,835,287,825
Operating income	6,614,750
Non-operating revenues and expenses:	
Legislative appropriations from the Commonwealth of Puerto Rico	313,000
Interest expense	(11,030,577)
Interest income	3,909,857
Total non-operating revenues, net of expenses	(6,807,720)
Decrease in net position	(192,970)
Net position at beginning of year	202,162,307
Net position at end of year	$ 201,969,337

See accompanying notes to financial statements.

Puerto Rico Health Insurance Administration
(A Component Unit of the Commonwealth of Puerto Rico)
Statement of Cash Flows
Fiscal Year ended June 30, 2019

	2019
	As restated
Cash flows from operating activities:	
Cash receipts from contributions	$ 2,742,351,069
Cash receipts from pharmacy rebate program	238,048,141
Cash payments of premiums, health care organizations and third party administrators	(2,729,638,545)
Cash payments to vendors and employees	(48,238,805)
Net cash provided by operating activities	202,521,860
Cash flows from non-operating and financing activities:	
Purchase of capital assets	(14,380)
Interest paid	(35,497)
Net cash used in non-operating and financing activities	(49,877)
Cash flows from investing activities:	
Interest collected	4,783,130
Advance premiums collected	21,261,602
Cash provided by investing activities	26,044,732
Net increase in cash and cash equivalents	228,516,715
Cash and cash equivalents, at beginning of year	54,922,769
Cash and cash equivalents, at end of year	$ 283,439,484

See accompanying notes to financial statements.

	2019 As restated
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 6,614,750
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization	1,022,764
Changes in operating assets and liabilities:	
Decrease (increase) in:	
Accounts receivable:	
Puerto Rico Department of Health	149,094,924
Municipalities	7,960,449
Pharmacy rebate program	(15,559,466)
Other receivables	(3,426,759)
Due from employers	422,024
Due from MCO's	5,463
Deferred outflows	2,466,266
Increase (decrease) in:	
TPA administration fees payable	13,600,654
Premiums and claims payable	52,906,616
Accounts payable and accrued expenses	4,773,235
Accrued termination benefits	(121,860)
Accrued compensated absences	(62,075)
Total pension liability	(14,955,385)
Deferred inflows	(2,219,740)
Net cash provided by operating activities	$ 202,521,860

See accompanying notes to financial statements.

1. REPORTING ENTITY

The ***Puerto Rico Health Insurance Administration*** (the Administration or PRHIA) is a governmental entity and a component unit of the Commonwealth of Puerto Rico (the Commonwealth), created on September 7, 1993 by Act No. 72 (the Act), as amended. The Administration commenced operations on February 1, 1994 and is considered a public corporation with full autonomy.

The Administration is responsible for implementing, administering and negotiating a health insurance system, through contracts with health insurers, mental health organizations, pharmacy benefit managers, third party administrators and Medicare Advantage organizations among others. The Administration thrives to provide all qualifying Puerto Rico residents access to quality healthcare services, including mental health, through a Managed Care Organization (MCO) model.

The Administration relies significantly on appropriations from the Commonwealth as well recurring and non-recurring federal funding. The Administration is the sub-grantee of federal funds provided by the Medicaid Program under Title XIX of the Social Security Act and Title XXI of the State Children's Health Insurance Program (CHIP). The Puerto Rico Department of Health (Department of Health) is the single state agency, and it has a cooperative agreement with the PRHIA which is responsible for implementing and administering the island-wide government health insurance program. Within the Department of Health, the Puerto Rico Medicaid Program (Medicaid Program) is the primary grantee of federal funds and is responsible for administering the eligibility to the government health insurance program of federal and Commonwealth beneficiaries.

A regionalization system was implemented to establish a network of participating providers throughout Puerto Rico and ensure the closest possible service to beneficiaries. The Administration pays a monthly premium to such insurance underwriters based on a contracted premium and the number of members subscribed in the health plan. Funds to pay for such premiums are requested from the Commonwealth net of funds available for such purposes from all other sources.

Under the provisions of Act No. 105 of July 19, 2002, which amended Act No. 72 of 1993, the Administration was authorized to negotiate directly with health providers under a pilot program. The Administration has, since then, entered into different direct contracts to cover the insured population of different regions and municipalities. Since November 1, 2006 through September 1, 2010, the Administration directly contracted providers that served approximately 190,000 lives from the metro-north region. Since June 30, 2011, the Administration has direct contracting projects with the Municipalities of Vieques and Guaynabo.

Effective October 1, 2010, a new integrated health care model named "Mi Salud" was developed with the following changes:

1) Set up a standard premium per region as established by the Administration.

2) Eliminate the referrals when the beneficiary needs the service of a specialist.

3) Better access to prescribed medicines without the authorization of the primary health care provider.

1. REPORTING ENTITY (CONTINUED)

4) Extended hours for health care providers of basic services

5) Tele-emergency services available 24 hours.

6) Integration of the physical and mental health care in one place.

7) The risk of the primary health provider in relation to medicines, emergency and preventive health care test was decreased and was transferred to the health care insurance companies.

8) Increase the coverage to include the middle-class working force.

9) Set up a ceiling in relation to administrative expenses and gains of the health care insurance companies.

On October 14, 2014, the Board of Directors of the PRHIA awarded new contracts for the Government Public Health Insurance Plan (the “GHP”), which replaced the former “Mi Salud” plan, to five private insurance providers pursuant to a bidding process. The new contracts became effective on April 1, 2015. Under the new contracts, the Commonwealth of Puerto Rico's public health insurance model changed from a Third-Party Administrator (TPA) model, in which the Commonwealth was ultimately responsible for the cost of the health services provided, to a MCO model, in which the Administration will pay the insurers a fixed premium for each insured beneficiary and the insurers will be responsible for the cost of such services.

On July 3, 2018, the Board of Directors of the Administration awarded new contracts for the new Government Healthcare Program to five private managed care organizations pursuant to a bidding process. Under the new model, beneficiaries will have the option to select the MCO and the network of providers of their choice. In addition, it will offer an enhanced care model for patients with certain chronic and high-cost, high-need (HCHN) conditions such as cancer, diabetes, end-stage renal disease, chronic obstructive pulmonary disease with asthma, hypertension, severe cardiac insufficiency, serious mental illness, and serious emotional disorder. Furthermore, the new model will strengthen oversight and the audit process with the creation of the Medicaid Fraud Control Unit and will also comply with the measures and cost-control objectives established in the Commonwealth’s fiscal plan.

2. GENERAL MATTER

On March 14, 2011, the Administration requested a $186 million non-revolving line of credit from the Government Development Bank of Puerto Rico (GDB). On the same date, a Fiscal Oversight Agreement (FOA) was subscribed between the Administration and GDB in order to provide assistance and monitoring of the Administration’s finances. The FOA authorizes GDB to assist the Administration to adopt a fiscal stabilization plan and to take measures it deems necessary to ensure the Administration’s financial self-sufficiency. The FOA was terminated by GDB as of June 30, 2018.

3. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Basis of Accounting

The accompanying financial statements have been presented on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Under this method, revenues are recognized when earned, regardless of when received, and expenses when incurred, regardless of when paid.

b. Basis of presentation

These financial statements are presented as an enterprise fund and conform to the provisions of Governmental Accounting Standards Board Statement No. 34 (GASB No. 34), Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. GASB No. 34, as amended, establishes standards for external financial reporting for all state and local governmental entities, which includes a Statement of Net Position, a Statement of Revenues, Expenses and Changes in Net Position and a Statement of Cash Flows.

c. Cash and cash equivalents

The Administration considers all highly liquid investments with maturities of three months or less to be cash equivalents.

d. Allowance for doubtful accounts

The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible losses on existing accounts receivable that may become uncollectible based on evaluations of collectability of accounts receivable and prior credit loss experience.

e. Capital assets

Capital assets are stated at cost. Donated property is reported at their estimated fair value at the date received. When assets are retired or otherwise disposed of, the cost and accumulated depreciation or amortization are removed from the accounts, and any resulting gain or loss is recorded for the period. Expenditures for repairs and maintenance that do not extend the useful lives of the assets are charged to operations in the year incurred.

3. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Impairment of Capital Assets

A capital asset generally should be considered impaired if both (a) the decline in service utility of the capital asset is large in magnitude and (b) the event or change in circumstance is outside the normal life cycle of the capital asset. The Administration reviews long-lived assets for impairment when circumstances indicate the carrying amount of an asset may not be recoverable. If the carrying amount of an asset may not be recoverable, a write-down to fair value is recorded. Long-lived assets are reviewed for impairment at the individual asset or the asset group level for which the lowest level of independent cash flows can be identified. No impairment charges were recorded during the year ended June 30, 2019.

g. Depreciation and amortization

Depreciation is provided over the estimated useful life of each class of depreciable asset which range from four to ten years and is computed using the straight-line method.

h. Compensated absences

The employees of the Administration earn thirty (30) days of vacation and eighteen (18) days of sick leave annually. Since May 2017, the employees accumulate 1.25 days per month of vacation, which is equivalent to 15 days of vacation annually. Vacation time accumulated is fully vested to the employees from the first day of work but cannot be used during the first three months of work. In the event of resignation, an employee is reimbursed for accumulated vacation days up to 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 after 10 years of services.

i. Deferred outflows/inflows of resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expenses/expenditure) until then. Net differences between projected and actual earnings on pension plan investments is deferred and recognized over a five-year period. Pension contributions made subsequent to the measurement date will be recognized as a reduction of the net pension liability after the next measurement date. Changes in proportional share of contributions, differences between the expected and actual experience and changes in actuarial assumptions, are capitalized and recognized over a period of time equal to the expected remaining working lifetime of active and inactive participants.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to future periods and so will not be recognized as inflows of resources (revenues) until that time.

3. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Net differences between projected and actual earnings on pension plan investments is deferred and recognized over a five-year period. Pension contributions made subsequent to the measurement date will be recognized as a reduction of the net pension liability after the next measurement date. Changes in proportional share of contributions, differences between the expected and actual experience and changes in actuarial assumptions, are deferred and recognized over a period of time equal to the expected remaining working lifetime of active and inactive participants.

j. Accounting for pension cost

Prior to July 1, 2017, the Administration accounted for pension costs under the provisions of GASB Statement No. 68, Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27, and GASB Statement No. 71, Pension Transitions for Contributions Made Subsequent to the Measurement Date, an amendment to GASB Statement No. 68. GASB Statement No. 68 required the Administration to report a net pension liability and related pension accounts, such as pension expense and deferred outflows/inflows of resources as determined by the Employee Retirement Systems of the Commonwealth of Puerto Rico (ERS), as applicable, under the requirements contained in GASB Statement No. 67, Financial Reporting for Pension Plans- an amendment to GASB Statement No. 25. Due to changes in the ERS, GASB 68 is no longer applicable to the Administration for the year ended June 30. 2019. Instead, the Administration adopted GASB 73. The Administration did not adopt GASB 75 because of its inmaterial effect.

k. Revenue recognition

The Administration distinguishes operating revenue from non-operating revenue. Revenue from sources from the Puerto Rico Department of Health, the Commonwealth of Puerto Rico, Municipalities, Employers and Pharmacy Rebate Program are recorded as operating revenue. Revenue from legislative appropriations and interest are recorded as non-operating revenue.

l. Contributions from the Commonwealth of Puerto Rico

Contributions received from the Commonwealth represent appropriations to cover the local share to meet federal funds matching requirements and funds for the payment of health insurance premiums and administrative expenses.

m. Contributions from the Puerto Rico Department of Health

Contributions received from the Department of Health represent payments to the Administration by the Medicaid Program which consist of a determined monthly amount of the funds allocated to Puerto Rico under Title XIX of the Social Security Act and State Plan.

To comply with the federal funds matching requirements, the Administration is assigned funds from the Commonwealth. The Medicaid Program is the recipient of CHIPS and Prescription Drugs funds which are in whole transferred to the Administration for health care services for the eligible population.

3. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

n. Contribution from Municipalities

Contribution from Municipalities represent the budgetary appropriations of the municipal governments for direct health services in areas covered by the government health plan. The charges made by the Administration are based on established percentages applied to the corresponding Municipalities' operational budget for the lesser of current fiscal year or fiscal year 2004-2005 as set forth in Act No. 72 of September 7, 1993, as amended. These contributions are withheld by the Center for Municipal Revenue Collection from money assigned to the municipalities and remitted to the Administration on a monthly basis. During fiscal year 2019 no contributions were required to be made due to the passing of law.

o. Pharmacy rebate program

The Administration established a governmental pharmacy rebate program which consists of agreements negotiated for obtaining pharmaceutical rebates and discounts with regards to the utilization of prescription branded drugs dispensed to beneficiaries. The Administration has continued engaging service organization for the pharmacy rebate program implementation and administration. The Administration retains 100 percent of the income derived from this program.

p. Use of estimates

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses. Such estimates primarily related to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from those estimates.

The employees have the right to accumulate the excess of sixty (60) days in vacation and ninety (90) days in sick leave until December 31 of each year. The excess should be used by the employee before the end of the following natural calendar year. The excess not used is forfeited.

Compensated absences are accrued when incurred using the pay or salary rates in effect at the date of the statement of net position.

q. Risk management

The Administration is exposed to various risks of loss from torts, theft of, damage to, and destruction of assets, errors and omissions, employee injuries and illnesses, natural disasters, and other losses. Commercial insurance coverage is obtained for potential claims arising from such matters.

The commercial insurance coverage is negotiated by the Department of Treasury of the Commonwealth of Puerto Rico and the cost is billed to the Administration.

3. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

r. Accounting Pronouncements issued but not yet effective

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. The requirements of this statement are effective for reporting periods beginning after December 15, 2019.

GASB Statement No. 88, Certain Disclosures Related to Debt

The primary objective of this statement is to improve the information that is disclosed in notes to government financial statements related to debt.

The requirements of this statement are effective for reporting periods beginning after December 15, 2019.

The Administration is evaluating the impact of these pronouncements.

4. CASH AND CASH EQUIVALENTS

The Administration's cash and cash equivalents as of June 30, 2019 consisted of the following:

	2019
Cash deposited in commercial banks	$ 283,436,902
Deposit account with the Government Development Bank for Puerto Rico	2,582
Total Cash and Cash Equivalents	$ 283,439,484

5. CUSTODIAL CREDIT RISK - DEPOSITS

Custodial credit risk is the risk that, in an event of a bank failure, the Administration deposits might not be recovered. The Commonwealth requires that public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance coverage. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth. Deposits at the GDB and the Economic Development Bank of Puerto Rico are uninsured and uncollateralized as these entities, which are component units of the Commonwealth, are exempt from compliance with the collateralization requirement.

At June 30, 2019 and 2018, the custodial risk of the Administration amounted to approximately $284 million and $56 million, respectively, which is the bank balance of cash and cash equivalents deposited in a financial institution and at the GDB. The balances are insured by the Federal Deposit Insurance Corporation up to $250,000. Deposits at the GDB are exempt from the collateral requirement established by the Commonwealth.

6. ACCOUNTS RECEIVABLE

Gross accounts receivable and the allowance for doubtful accounts as of June 30, 2019 consist of the following:

	2019
Puerto Rico Department of Health	$ 347,409,848
Municipalities	89,156,413
Legislature appropriations and other	12,550,927
Pharmacy rebates program	75,262,242
Other receivables	414,920
Due from employers	107,639,530
	632,433,880
Allowance for doubtful accounts - Municipalities	(89,156,413)
Allowance for doubtful accounts - Legislature appropriations and other	(744,520)
Allowance for doubtful accounts - Due from employers	(107,390,496)
	(197,291,429)
Accounts receivable, net	$ 435,142,451

Accounts receivable consist of financial assistance from the federal Medicaid Program and the corresponding state contributions and legislature appropriations. In addition, the administration has receivables from its pharmacy rebates program, employers' contributions, and other contributions. Accounts receivable are stated net of an allowance for doubtful accounts. The Administration estimated the allowance based on its historical experience of the relationship between actual collection and billings.

7. DUE FROM MCO's

The Administration contracted the services of a public accounting firm to carry out an internal audit of the claims payment system under the previous TPA model. The sample selected for testing revealed that the Administration made duplicated payments and paid premiums for deceased members to the contracted health insurance entities under such model.

The overpayment amount was estimated by first, matching the certified deceased records to the Administration active enrollment file. Then, for each matching record, the Administration computed the number of months after the date of death for which a premium was paid by the corresponding PMPM payment.

As a result of the audit, the Administration filed a claim to one of the health insurance entities representing 37% of the total overpayment. As of the date of this report various validation procedures have been satisfactorily performed over the underlying data, but other allegations brought by the counterparty challenging certain contractual aspects of the GHP contract remain unresolved. The Administration believes that it has conclusive evidence to overcome counterparty allegations and recover a part of the amount claimed. As of June 30, 2019, the allowance for doubtful accounts of the above-mentioned overpayment was established for approximately $10.6.

8. CAPITAL ASSETS

The activities of the capital assets accounts for the fiscal year ended June 30, 2019 were as follows:

	June 30, 2019			
	Beginning Balance	Additions	Retirements	Ending
Equipment, computer and software	$ 3,056,432	$ 12,503	$ -	$ 3,068,935
Leasehold improvements	179,829	-	-	179,829
Furniture and others	1,148,244	1,878	-	1,150,122
	4,384,505	14,381	-	4,398,886
Accumulated depreciation	(2,006,331)	(1,022,764)	-	(3,029,095)
Capital assets, net	$ 2,378,174	$ (1,008,383)	$ -	$ 1,369,791

9. OBLIGATION PAYABLE GOVERNMENT DEVELOPMENT BANK

On March 14, 2011, the Administration entered into a Credit Agreement with the Government Development Bank for Puerto Rico in order to pay its obligations to healthcare insurers incurred prior to fiscal year 2009-2010. The aggregate principal amount of the non-revolving line of credit was $186,000,000, payable in nine payments of $20,666,667, and each due on March 14 of the years 2015 through 2023. Interest is accrued at a fluctuating annual rate equal to the greater of (i) 1.5% over prime rate, and (ii) 6%.

As of June 30, 2019, the outstanding principal balance amounted to $183,251,298 and the accrued interest amounted to $52,698,420. The Administration will pay the principal and interest with appropriations to be received from the Legislature of Puerto Rico through the Puerto Rico Office of Management and Budget (OMB) pursuant to Act No. 173. Notwithstanding, during the fiscal year ended June 30, 2019, the OMB failed to make principal and interest payments on behalf of the Administration. OMB did not appropriate any funds to pay the principal and interest of this Credit Agreement.

On July 20, 2016, the Governor of Puerto Rico signed the Law 74 which authorized the GDB to consolidate all financing agreements made to governmental entities which are payable with appropriations from the legislature. Article 4 of such law lists all the governmental entities with financial agreements and the outstanding principal balance and accrued interest as of December 31, 2015. The Administration is listed with an outstanding principal balance of $183,251,298 and accrued interest of $14,215,650 as of December 31, 2015.

10. RETIREMENT SYSTEM

Plan description

The Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (the ERS), created pursuant to Act No. 447 of May 15, 1951, as amended, is a cost-sharing multiple-employer defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth. The ERS is a pension trust fund of the Commonwealth. All regular employees of the Administration hired before January 1, 2000 and less than fifty-five (55) years of age at the date of employment became members of the ERS as a condition to their employment. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

The ERS administers different benefit structures pursuant to Act No. 447, as amended, including a cost-sharing, multi-employer, Defined Benefit Program, a Defined Contribution Program (System 2000 program) and a Contributory Hybrid Program. Benefit provisions vary depending on a member's date of hire. Substantially all full-time employees of the Commonwealth and its instrumentalities (73 Commonwealth agencies, 78 municipalities, and 55 public corporations) are covered by the ERS. Membership is mandatory for all regular, appointed, and temporary employees of the Commonwealth and the Commonwealth's public corporation at the date of employment. Membership is optional for the Governor of the Commonwealth, Commonwealth secretaries, head of public agencies and instrumentalities, among others.

10. RETIREMENT SYSTEM (CONTINUED)

The benefits provided to members of the ERS are established by Commonwealth law and may be amended only by the Legislature with the Governor's approval. Act No. 3 of April 4, 2013 (Act No. 3), in conjunction with other recent funding and design changes, provided for a comprehensive reform of the ERS. Certain provisions are different for the three groups of members who entered the ERS prior to July 1, 2013 as described below:

- Members of Act No. 447 are generally those members hired before April 1, 1990.
- Members of Act No. 1 of February 16, 1990 (Act No. 1) are generally those members hired on or after April 1, 1990 and on or before December 31, 1999.
- Members of Act No. 305 of September 24, 1999 (Act No. 305 or System 2000) are generally those members hired on or after January 1, 2000 and on or before June 30, 2013.

All regular employees hired for the first time on or after July 1, 2013, and former employees who participated in the defined benefit program and the System 2000 program, and were rehired on or after July 1, 2013, become members of the Contributory Hybrid Program as a condition to their employment. In addition, employees who at June 30, 2013, were participants of previous programs became part of the Contributory Hybrid Program on July 1, 2013.

Each member has a nonforfeitable right to the value of his/her account. Members have three options to invest their contributions. Investment income is credited to the member's account semi-annually. The Commonwealth does not guarantee benefits at retirement age.

The assets of the Defined Benefit Program, the Defined Contribution Program and the Contributory Hybrid Program are pooled and invested by ERS. Future benefit payments will be paid from the same pool of assets. In addition, employers' contributions for members hired on or after January 1, 2000 will be used by ERS to reduce the unfunded status of the Defined Benefit Program.

This summary of ERS plan provisions is intended to describe the essential features of the plan. All eligibility requirements and benefit amounts should be determined in strict accordance with the plan document itself.

<u>Service retirement eligibility requirements</u>

a) Eligibility for Act No. 447 Members: Act No. 447 members who were eligible to retire as of June 30, 2013 would continue to be eligible to retire at any time. Prior to July 1, 2013, Act No. 447 members could retire upon (1) attainment of age 55 with 25 years of credited service, (2) attainment of age 58 with 10 years of credited service, (3) any age with 30 years of credited service, (4) for Public Officers in High Risk

Date of birth	**Attained age as of June 30, 2013**	**Retirement eligibility age**
July 1, 1957 or later	55 or less	61
July 1, 1956 to June 30, 1957	56	60
Before July 1, 1956	57 and up	59

10. RETIREMENT SYSTEM (CONTINUED)

In addition to the requirements in the table above, Act No. 447 Public Officers in High Risk Positions who were not eligible to retire as of June 30, 2013 and did not attain 30 years of credited service by December 31, 2013 are eligible to retire directly from active service upon the attainment of age 55 with 30 years of credited service.

b) Eligibility for Act No. 1 Members: Act No. 1 members who were eligible to retire as of June 30, 2013 continue to be eligible to retire at any time. Prior to July 1, 2013, Act No. 1 members could retire upon (1) attainment of age 55 with 25 years of credited service, (2) attainment of age 65 with 10 years of credited service, (3) for Public Officers in High Risk Positions, any age with 30 years of credited service, and (4) for Mayors, attainment of age 50 with 8 years of credited service as a Mayor.

Act No. 1 members who were not eligible to retire as of June 30, 2013 are eligible to retire upon attainment of age 65 with 10 years of credited service. In addition, Act No. 1 Public Officers in High Risk Positions who were not eligible to retire as of June 30, 2013 are eligible to retire directly from active service upon the attainment of age 55 with 30 years of credited service.

c) Eligibility for System 2000 Members: System 2000 members who were eligible to retire as of June 30, 2013 continue to be eligible to retire at any time. Prior to July 1, 2013, System 2000 members could retire upon attainment of age 55 for Public Officers in High Risk Positions and attainment of age 60 otherwise.

System 2000 members who were not eligible to retire as of June 30, 2013 are eligible to retire upon attainment of age 55 for Public Officers in High Risk Positions and upon attainment of the retirement eligibility age shown in the table below otherwise.

Date of birth	Attained age as of June 30, 2013	Retirement eligibility age
July 1, 1957 or later	55 or less	65
July 1, 1956 to June 30, 1957	56	64
July 1, 1955 to June 30, 1956	57	63
July 1, 1954 to June 30, 1955	58	62
Before July 1, 1954	59 and up	61

d) Eligibility for Members Hired after June 30, 2013: Attainment of age 58 if a Public Officer in a High-Risk Position and attainment of age 67 otherwise.

<u>Service Retirement Annuity Benefits:</u>

An annuity payable for the lifetime of the member equal to the annuitized value of the balance in the hybrid contribution account at the time of retirement, plus, for Act No. 447 and Act No. 1 members, the accrued benefit determined as of June 30, 2013. If the balance in the hybrid contribution account is $10,000 or less, it shall be paid as a lump sum instead of as an annuity.

1) *Accrued Benefit as of June 30, 2013 for Act No. 447 Members* – The accrued benefit as of June 30, 2013

10. RETIREMENT SYSTEM (CONTINUED)

shall be determined based on the average compensation, as defined, for Act No. 447 members, the years of credited service, and the attained age of the member all as of June 30, 2013. For Act No. 447 Mayors, the highest compensation, as defined, as a Mayor is determined as of June 30, 2013.

If the Act No. 447 member had at least 30 years of credited service as of June 30, 2013, the accrued benefit equals 65% of average compensation if the member was under age 55 as of June 30, 2013 or 75% of average compensation if the member was at least age 55 as of June 30, 2013. For participants selecting to coordinate with social security (the Coordination Plan), the benefit is re-calculated at the Social Security Retirement Age (SSRA), as defined, as 1.5% of average compensation up to $6,600 multiplied by years of credited service, up to 30 years, plus 65% (75% if member was at least age 55 as of June 30, 2013) of average compensation in excess of $6,600.

If the Act No. 447 member had less than 30 years of credited service as of June 30, 2013, and attains 30 years of credited service by December 31, 2013, the accrued benefit equals 55% of average compensation if the member was under age 55 as of June 30, 2013 or 60% of average compensation if the member was at least age 55 as of June 30, 2013. For participants selecting the Coordination Plan, the benefit is re-calculated at SSRA as 1.5% of average compensation up to $6,600 multiplied by years of credited service, up to 30 years, plus 55% (60% if member was at least age 55 as of June 30, 2013) of average compensation in excess of $6,600. Member contributions received from Act No. 447 members eligible for this transitory benefit during the period beginning July 1, 2013 and ending upon the attainment of 30 years of credited service are considered pre-July 1, 2013 contributions; the contributions to the hybrid contribution account begin after the member attains 30 years of credited service.

If the Act No. 447 member had less than 30 years of credited service as of December 31, 2013, the accrued benefit equals 1.5% of average compensation multiplied by years of credited service up to 20 years, plus 2% of average compensation multiplied by years of credited service in excess of 20 years.

Maximum benefit is 75% of average compensation. Except for Commonwealth Police and Commonwealth Firefighters, the benefit is actuarially reduced for each year payment commences prior to age 58. For participants selecting the Coordination Plan, the basic benefit is re-calculated at SSRA as 1% of average compensation up to $6,600 multiplied by years of credited service up to 20 years, plus 1.5% of average compensation up to $6,600 multiplied by years of credited service in excess of 20 years, plus 1.5% of average compensation in excess of $6,600 multiplied by years of credited service up to 20 years, plus 2.0% of average compensation in excess of $6,600 multiplied by years of credited service in excess of 20 years. Except for Police and Firefighters, the benefit is actuarially reduced for each year payment commences prior to age 58.

For Act No. 447 Mayors with at least 8 years of credited service as a mayor, the accrued benefit will not be less than 5% of highest compensation, as defined, as a Mayor for each year of credited service as a Mayor up to 10 years, plus 1.5% of highest compensation as Mayor for each year of non-Mayoral credited service up to 20 years, plus 2.0% of highest compensation as Mayor for each year of non-Mayoral credited service in excess of 20 years. Non-Mayoral credited service includes service earned as a Mayor in excess of 10 years. Maximum benefit is 90% of highest compensation as a Mayor.

10. RETIREMENT SYSTEM (CONTINUED)

2) *Accrued Benefit as of June 30, 2013 for Act No. 1 Members* – The accrued benefit as of June 30, 2013 shall be determined based on the average compensation for Act No. 1 members, the years of credited *service*, and the attained age of the member all as of June 30, 2013. For Act No. 1 Mayors, the highest compensation as a Mayor is determined as of June 30, 2013.

   If the Act No. 1 member is a police officer or firefighter with at least 30 years of credited service as of June 30, 2013, the accrued benefit equals 65% of average compensation if the member was under age 55 as of June 30, 2013 or 75% of average compensation if the member was at least age 55 as of June 30, 2013.

   For all other Act No. 1 members, the accrued benefit equals 1.5% of average compensation multiplied by years of credited service. The benefit is actuarially reduced for each year payment commences prior to age 65.

   For Act No. 1 Mayors with at least 8 years of credited service as a Mayor, the accrued benefit will not be less than 5% of highest compensation as a Mayor for each year of credited service as a Mayor up to 10 years, plus 1.5% of highest compensation as Mayor for each year of non-Mayoral credited service up to 20 years, plus 2.0% of highest compensation as Mayor for each year of non-Mayoral credited service in excess of 20 years. Non-Mayoral credited service includes service earned as a Mayor in excess of 10 years. Maximum benefit is 90% of highest compensation as a Mayor.

Compulsory Retirement

All Act No. 447 and Act No. 1 Public Officers in High Risk Positions must retire upon attainment of age 58 and 30 years of credited service. A two-year extension may be requested by the member from the Superintendent of the Puerto Rico Police, the Chief of the Firefighter Corps, or supervising authority as applicable.

Contributions

1) *Member Contributions*

   Effective July 1, 2013, contributions by members are 10% of compensation. However, for Act No. 447 members who selected the Coordination Plan, the member contributions are 8.5% of compensation up to $6,600 plus 10% of compensation in excess of $6,600 during the 2013-2014 fiscal year and 8.5% of compensation up to $6,600 plus 10% of compensation in excess of $6,600 during the 2013-2014 fiscal year. Members may voluntarily make additional contributions to their hybrid contribution account.

10. RETIREMENT SYSTEM (CONTINUED)

2) *Employer Contributions (Article 2-116, as Amended by Law No. 116 of 2010 and Act No. 3)*

   Effective July 1, 2011, employer contributions are 9.275% of compensation. For the next four fiscal years effective July 1, employer contributions will increase annually by 1% of compensation. For the five fiscal years thereafter, employer contributions will increase annually by 1.25% of compensation, reaching an employer contribution rate of 20.525% of compensation effective July 1, 2020.

3) *Supplemental Contributions from the Commonwealth's General Fund, Certain Public Corporations, and Municipalities (Act No. 3)*

   Effective July 1, 2013, the ERS will receive a supplemental contribution of $2,000 (of which $800 corresponds to the pension plan and $1,200 corresponds to the post employment healthcare benefits plan) each fiscal year for each pensioner (including beneficiaries receiving survivor benefits) who was previously benefitting as an Act No. 447 or Act No. 1 member while an active employee. This supplemental contribution will be paid by the Commonwealth's General Fund for former government and certain public corporations without own treasuries employees or by certain public corporations with own treasuries or municipalities for their former employees.

4) *Additional Uniform Contribution (Act No. 32, as amended)*

   The additional uniform contribution will be certified by the external actuary of the ERS each fiscal year from 2014–2015 through 2032–2033 as necessary to avoid having the projected gross assets of the ERS, during any subsequent fiscal year, to fall below $1 billion. The additional uniform contribution is to be paid by the Commonwealth's General Fund, public corporations with own treasuries, and municipalities.

Additional information on the ERS is provided in its stand-alone basic financial statements, a copy of which can be obtained from the ERS Administration, PO Box 42003, San Juan, PR 00949.

On October 30, 2016, the Fiscal Oversight Board for Puerto Rico designated the Government of Puerto Rico, the ERS for Government Employees, the Judicial ERS, and the Teacher ERS (together the "ERSs"), the University of Puerto Rico and 21 other public corporations of Puerto Rico as covered entities, subject to fiscal supervision in accordance with the federal legislation Puerto Rico Oversight, Management, and Economic Stability Act, better known as PROMESA.

Due to the lack of projected liquidity of the ERSs, the Government of Puerto Rico will protect payments to pensioners. Effective July 1, 2017, the Government of Puerto Rico adopted the "PayGo" system. Under this new system, the Government will be responsible for paying the deficiency of the ERSs to provide retirement benefits for the pensioners.

Also, as of July 1, 2017, employer contributions, contributions under special laws and the Uniform Additional Contribution (Law no. 32-2013) will be eliminated and replaced with the "PayGo". Currently, the Government of Puerto Rico is working on reforming the ERSs from its current form to a New Defined Contribution Plan managed by a private entity.

10. RETIREMENT SYSTEM (CONTINUED)

Accordingly, the Puerto Rico Department of the Treasury will bill government agencies, public corporations, municipalities, the executive branch, the legislative branch and the judicial branch (together the "Government Agencies") a monthly charge to cover the retirement benefits to their pensioners. The ERSs will determine and administer the amount of the payment by pensioner that will correspond to each of the Government Agencies. This charge is known as the "PayGo".

Total employer contributions for the year ended June 30, 2019, amounted to approximately $357,000.

Total Pension Liability and Actuarial Information

The total pension liability was approximately $5.5 million as of June 30, 2019. The total pension liability as of June 30, 2018 was determined by an actuarial valuation as of July 1, 2017 which was rolled forward to June 30, 2018 (measurement date as of June 30, 2018).

Actuarial Methods and Assumptions

The actuarial valuation used the following actuarial assumptions applied to all periods in the measurement period.

Discount Rate

The discount rate for June 30, 2018 was 3.87%. This represents the municipal bond return rate as chosen by the Commonwealth. The source is the Bond Buyer Go 20-Bond Municipal Bond Index, which includes tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher.

Mortality

The mortality tables used in the June 30, 2018 actuarial valuation were as follows:

--Pre-retirement Mortality

For general employees not covered under Act No. 127, RP-2014 Employee Mortality Rates for males and females adjusted to reflect Mortality Improvement Scale MP-2019 from the 2007 base year and projected forward using MP-2019 on a generational basis. For members covered under Act No. 127, RP-2014 Employee Mortality Rates are assumed with blue collar adjustments for males and adjusted to reflect Mortality Improvement Scale MP-2019 from the 2006 base year and projected forward using MP-2019 on a generational basis. As generational tables, they reflect mortality improvements both before and after the measurement date.

10. RETIREMENT SYSTEM (CONTINUED)

100% of deaths while in active service are assumed to be occupational for members covered under Act 127.

-- Post-retirement Healthy Mortality

Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of the Plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 92% of the rates from the UP-1994 Mortality Table for Males and 95% of the rates from the UP-1994 Mortality Table for Females, both projected from 1994 to 2010 using Scale AA. The base rates are projected using Mortality Improvement Scale MP-2019 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

-- Post-retirement Disable Mortality

Rates which vary by gender are assumed for healthy retirees and beneficiaries based on a study of the Plan's experience from 2007 to 2012 and updated expectations regarding future mortality improvement. The 2010 base rates are equal to 105% of the rates from the UP-1994 Mortality Table for Males and 115% of the rates from the UP-1994 Mortality Table for Females. The base rates are projected using Mortality Improvement Scale MP-2019 on a generational basis. As a generational table, it reflects mortality improvements both before and after the measurement date.

Other Assumptions as of June 30, 2018

Actuarial cost method	Entry age normal
Inflation rate	Not applicable
Salary increases	3.00% per year. No compensation increases are assumed until July 1, 2021 as a result of Act No. 3-2017, four-year extension of Act No. 66-2014, and the current general economy

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

The following presents the total pension liability calculated using the discount rate of 3.87%, as well as what it would be if it were calculated using the discount rate of 1-percentage point lower (2.87%) or 1-percentage-point higher (4.87%) than the current rate:

	At 1% decrease (2.87%)	At current discount rate (3.87%)	At 1% increase (4.87%)
Total Pension Liability	$ 6,314,638	$ 5,549,379	$ 4,928,237

10. RETIREMENT SYSTEM (CONTINUED)

Deferred Outflows of Resources and Deferred Inflows of Resources

The following presents a summary of changes in the deferred outflows of resources and deferred inflows of resources (excluding employer specific amounts) for the year ended June 30, 2019:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Pension benefits paid subsequent to measurement date	$ 356,574	$ -
Difference between expected and actual experience in measuring the total pension liability		167,842
Changes in assumptions		181,976
Change in employer's contributions and employer's proportionate share of contributions	368,180	-
Total	$ 724,754	$ 349,818

Pension Benefit

For the fiscal year ended June 30, 2019, ASES recognized pension benefit of approximately 14.7 million. Pension benefit represents the change in the total pension liability during the measurement period, adjusted for actual contributions and the deferred recognition of changes in investment gain/loss, actuarial gain/loss, actuarial assumptions or method, and plan benefits.

Total Pension Liability

ASES's Total Pension Liability for each plan program is measured as the proportionate share of the Total Pension Liability. The Total Pension Liability of each of the plan program was measured as of June 30, 2019, and the Total Pension Liability for each plan program used to calculate the Total Pension Liability was determined by an actuarial valuation as of June 30, 2019. ASES proportion of the Total Pension Liability was based on a projection of the ASES's long-term share of contributions to the pension plans program relative to the projected benefits paid of all participating employers, actuarially determined. As June 30, 2019, ASES used the proportional share of .02266%.

10. RETIREMENT SYSTEM (CONTINUED)

Total Pension Liability (continued)

As June 30, 2019, ASES reported $5,549.379 as Total Pension Liability for its proportionate share of the Total Pension Liability of ERS as follows:

	June 30, 2018	
	Total	Proportional Share .02266%
Total Pension Liability	$ 24,489,519,237	$ 5,549,379

The financial statements and required supplementary information for the pension plan are available at the administration of the Employee's Retirement System (ERS) of the Commonwealth of Puerto Rico, P.O. Box 42003, San Juan, PR 00940-2203.

11. EARLY 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 Administration. Act No. 70 established that early retirement benefits will be provided to eligible employees that have completed between 15 to 29 years of creditable services 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 Administration will pay the employer contributions to the Retirement System and the corresponding pension until the employee complies with the age requirements and 30 years of creditable services applicable to the Retirement System. Economic incentives are available to eligible employees that qualify for retirement benefits. Economic incentives consist of a payment ranging from one to six months of salary. Additionally, eligible employees that choose to participate in this program, other than those qualifying for retirement benefits, are eligible to receive health plan coverage for up to 12 months in a health plan selected by management of the Commonwealth of Puerto Rico.

At June 30, 2019, unpaid long-term benefits granted on this program were discounted 3%. Total accrued terminations benefit as of June 30, 2019 amounted to approximately $3,623,000.

12. COMMITMENT AND CONTINGENCIES

Commitments

On July 1, 2014, the Administration signed a lease agreement for five years commencing on July 1, 2014 through June 30, 2019 with an automatic extension for another five years from July 1, 2019 through June 30, 2024. The lease agreement has a cancellation penalty of $950,000 if the lease is not renewed at the end of the five-year term. Rent expense was approximately $389,000 for fiscal year ended June 30, 2019.

Total future minimum lease payments on this operating lease as of June 30, 2019, are as follows:

Year ending June 30,	**Amount**
2020	$ 400,375
2021	412,454
2022	412,454
2023	412,454
2024	412,454
	$ 2,050,191

Contingencies

The Administration is defendant and/or co-defendant in legal proceedings pertaining to matters incidental to the performance of its operations. With respect to the pending and threatened litigations, the Administration, in consultation with legal counsel, has advised that at this stage of the proceedings they cannot offer an opinion as to the probable outcome. Accordingly, management does not consider necessary making any provision in its books for these cases and intends to contest them vigorously.

Federal grants

The Administration receives as a sub-grantee financial assistance from the federal government corresponding to Medicaid Program passed through the Puerto Rico Department of Health, the grantee. Federal grants are subject to financial and compliance audits by grantor agencies to determine the Administration’s compliance with the regulations and conditions of such grants. It is management’s opinion that no additional material unrecorded liabilities will arise from audits previously performed or to be performed.

13. RESTATEMENT

The Administration is restating its financial statements for the year ended June 30, 2019 to correct various account balances related to the adoption of GASB Statement No. 73 as summarized below:

Pension benefit	$ (14,708,859)
Deferred outflows related to pension plan	$ (2,466,266)
Deferred inflows related to pension plan	$ 2,219,740
Total pension liability	$ 14,955,385

14. SUBSEQUENT EVENTS

The Administration has evaluated all subsequent events through September 8, 2020, which is the date the financial statements were available to be issued.

In July 2019, the Administration's ex Executive Director (had resigned on June 25, 2019), Mrs. Angela Avila, was arrested and charged with conspiring to favor a consulting firm in obtaining contracts with the Administration. Upon occurrence of this event such contracts were duly cancelled.

The Administration has considered the consequences of COVID-19, and has determined that it does not create an uncertainty on future performance.