FINANCIAL STATEMENTS, OTHER FINANCIAL INFORMATION (UNAUDITED) AND OTHER REPORT

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)
Years Ended September 30, 2012 and 2011
With Report of Independent Auditors

Ernst & Young LLP

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Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Financial Statements, Other Financial Information
and Other Report

Years Ended September 30, 2012 and 2011

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Report of Independent Auditors

The Board of Directors
Virgin Islands Port Authority

We have audited the accompanying basic financial statements of the Virgin Islands Port Authority (the Authority), a component unit of the Government of the U.S. Virgin Islands, as of and for the years ended September 30, 2012 and 2011, as listed in the table of contents. 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Authority's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Virgin Islands Port Authority as of September 30, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 8, 2013, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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Accounting principles generally accepted in the United States require that the management's discussion and analysis on pages 3 through 15 be presented to supplement the basic financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audit of the 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.

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Authority's basic financial statements. The other financial information and related notes, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and accordingly, we do not express an opinion or provide any assurance on it.

Ernst & Young LLP

July 8, 2013

The purpose of the following management's discussion and analysis of the financial performance and activity of the Virgin Islands Port Authority (the Authority) is to help the readers understand the basic financial statements of the Authority for the years ended September 30, 2012 and 2011, with selected comparative information for the year ended September 30, 2010. This discussion has been prepared by management and should be read in conjunction with the basic financial statements and the notes thereto, which follow this section.

Reporting Entity

The Authority is a public corporation and an autonomous governmental instrumentality of the Government of the U.S. Virgin Islands. The Authority owns and operates the air and marine terminals of the U.S. Virgin Islands through two operating divisions, Aviation and Marine.

The Aviation Division manages two airport facilities, the Cyril E. King Airport (CEKA) located on the island of St. Thomas and the Henry E. Rohlsen Airport (HERA) located on the island of St. Croix. The Aviation Division's revenues consist mainly of landing and passenger fees and rental income. The Aviation Division also generates a small amount of revenues from the leases of a housing complex and certain properties outside the airport facilities, which are known as Special Facilities.

The Marine Division is responsible for the maintenance and operation of marine cargo and passenger facilities in St. Thomas, St. Croix and St. John. Revenues are mostly derived from charges to cruise ship lines and cargo lines, including property rental fees.

Using the Financial Statements

The Authority's financial report includes three financial statements: the Statement of Net Assets, the Statement of Revenues, Expenses and Changes in Net Assets and the Statement of Cash Flows. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the *Government Accounting Standards Board* (GASB).

Financial Highlights

Operating Revenues

The total operating revenues for the Virgin Islands Port Authority for fiscal years 2012 and 2011 are $47.2 million and $46.5 million, respectively. The fluctuation in operating revenues when compared to fiscal year 2011 is an increase of approximately $700 thousand, or 1.5% in operating revenues. The Aviation Division recorded an increase of approximately 4.4% in revenues in 2012 when compared to 2011. Additionally, 2012 marine revenues decreased by approximately 0.8% when compared to 2011.

The 2012 increase in revenues under the aviation division of 4.4% resulted from an overall increase of 9.9% in passenger traffic when compared to 2011; comprised of an increase of 62,747 passengers at Cyril E. King Terminal and 20,232 passengers at the Henry E. Rohlsen Airport Terminal in St. Croix, and an 8.9% increase in arriving passengers comprised of 54,502 passengers at Cyril E. King Terminal and 20,175 passengers at the Henry E. Rohlsen Terminal. The total increase in passenger traffic is credited for the increase in revenues for aviation operating revenues Users' fees and dues. Rental revenues showed an increase of 2.1%. In this category Other Building Rental and Other Rental declined 12% and 6%, respectively, while Counter Space Rental and Land Rental increased 31% and 12%, respectively. Hanger Rental and Office Space Rental each showed a 3% and 4% increase, respectively. Other fees increased approximately 11.6% resulting from a notable increase of 78% in Tour Vehicle Fees which was a fee added in 2011 and increases in Restaurant Commissions and Liquor Concessions of 32% and 20%, respectively. As a result of increased passenger traffic; most concessions related to passenger activity were positively affected.

In the Marine Division, revenues decreased due to decreases in passenger activity and cruise calls to the port of St. Thomas, although there were calls to the island of St. Croix, no fees were collected from cruise lines. In 2012, cruise passengers decreased by 62,812 when compared to fiscal year 2011. Wharfage dues showed a 5.8% increase; consisting of a 14% increase in Passenger Wharfage attributed to the 15% administrative fee charged on the collections of the Marine Terminal Tax passed by the Legislature which became effective in January 2012. Rentals decreased 3.3% partly attributed to a fire at our Subbase #18 property which caused displacement of 3 tenants at that location with a 47% decrease in Other Building Rental, Land Rental and Office Space Rental each showed a 5% and 3% decrease, respectively. Other marine activity includes: decreases for Fuel Commission and Fees 54%, and Demurrage 690%, Other Commission and Fees 37%; and increases for Auto Rental Commissions 67%, Restaurant Commissions 15% and Parking Commissions 6%.

The 2011 decrease in revenues under the Aviation Division of 2.9% resulted from an overall decrease of 27,063 in passenger traffic from 2010; comprised of a 21,566 decrease at Cyril E. King Terminal and a 5,497 decrease at the Henry E. Rohlsen Airport Terminal in St. Croix. The total decrease in passenger traffic is credited for the decrease in revenues for aviation operating revenues Users' Fees and Dues. Rental revenues showed a small increase of .2%, Gift Shops, Rental declined 11%, Space Rental Liquor Concessions & Other Building Rental increased 7% and 8%, respectively, and Cargo Building and Cocktail Lounge increased 4% and 3%, respectively. Other fees decreased approximately .9% resulting from a notable decline of 19% in liquor concessions and an increase in Other Commissions and Fees of 25%. As a result of the reduction in passenger traffic concessions revenues were negatively affected.

In the Marine Division, revenues increased mainly due to increases in passenger activity and cruise calls to the port of St. Thomas, although there were calls to the island of St. Croix, no fees were collected from cruise lines. In 2011, cruise passengers increased by 192,882 over fiscal year 2010. Austin Babe Monsanto (ABM) experienced an increase in passenger activity due to increased cruise calls to the facility. Rental decreases were more significant at the Austin Babe Monsanto (ABM) Facility (Crown Bay) due to the maturity of the temporary lease rental of the restaurant building. To date ABM does not remain 100% occupied in tenancy, new tenants are constantly being sought for the facility; most recently the largest vacancy was leased; the lease will positively affect revenues and facility usage in the upcoming fiscal year and beyond. Other marine activity included increases for car ferry activities of 27%, tour vehicles of 39%, parking fees of 19%, fuel commission and fees of 42%, and demurrage of 390%.

The following table details the components of and changes in operating revenues:

(In thousands of dollars)	2012	2011	2010	Change 2012	Change 2011
Aviation operating revenues:					
Users' fees and dues	**$ 12,519**	$ 12,116	$ 12,708	$ 403	$ (592)
Rentals	**4,970**	4,867	4,855	103	12
Others	**3,890**	3,485	3,518	404	(33)
Total Aviation operating revenues	**21,379**	20,468	21,081	910	(613)
Marine operating revenues:					
Users' fees and dues	**14,064**	14,482	13,082	(418)	1,400
Wharfage dues	**5,916**	5,591	4,808	325	783
Rentals	**4,853**	5,019	4,925	(166)	94
Others	**1,018**	976	949	42	27
Total Marine operating revenues	**25,851**	26,068	23,764	(217)	2,304
Total operating revenues	**$ 47,230**	$ 46,536	$ 44,845	$ 693	$ 1,691

Wharfage and Tonnage

The U. S. Virgin Islands is defined as a territory of the United States and as such is authorized by Congress to set its own custom duties. The revenue generated from custom duties is intended to assist the Government of the Virgin Islands operations. Through a Memorandum of Agreement (MOA) signed in 1994 by the Government of the Virgin Islands (GVI) and Customs (now Custom Border and Protection “CBP”), the latter was authorized to collect the USVI custom duties and the wharfage and tonnages port user fees of the Virgin Islands Port Authority (VIPA). The MOA required CBP to pay the revenue to the USVI treasury, less CBP’s cost of collecting both the custom duties and wharfage and tonnage user fees of the VIPA, at which point the GVI charges a 5% administrative fee for processing a check to the VIPA.

The Virgin Islands Port Authority assesses fees through its tariff to users for use of its wharfs and for tonnage based on cargo capacity. The Authority charges such fees to enable it to maintain the various marine facilities for expenses such as dredging, repairs and maintenance and replacement of facilities as needed.

Over time, the CBP's cost for collecting has exceeded the amount of both the custom duties and port user fees collected. CBP's costs charged to the USVI have doubled from an average of $7.2 million per year for fiscal years 1998-2003 to an average of $14.3 million per year for fiscal years 2004-2009. This has directly impacted the amounts available to remit to the GVI and the VIPA.

At the close of fiscal year 2009, VIPA had $6,160,026 due from CBP. Currently, that amount is in dispute and accordingly VIPA wrote off the receivable related to charges for the period from February 2008 through September 2009. The write-off exacerbated VIPA's operating loss to $16 million at the close of fiscal year 2009. For fiscal year 2012 VIPA has written off the receivables related to charges for Fiscal Year 2010 and 2011 in the amount of $3,450,354.

Moving forward, the GVI has removed VIPA from the MOA. Effective March 1, 2011, VIPA commenced collecting an equivalent tariff for the former wharfage and tonnage under the new categorization of harbor use fee and facility use fee. VIPA will continue to pursue the outstanding receivable from CBP and will recognize the revenue when and if received.

Operating Expenses

Fiscal year 2012 operating expenses for the Virgin Islands Port Authority decreased approximately 3.7% in comparison to 0.3% increase in fiscal year 2011. Payroll, taxes and fringe benefits decreased by 1.6%. Fiscal year 2011 payroll cost included accruals for increases awarded through contractual agreements to the marine union dating back from fiscal year 2007 through fiscal year 2011.

The Authority continued to pay 100% of medical insurance for all employees during fiscal year 2012. Although the Authority has negotiated with most of its unions to share 15% of the medical insurance, the agreement with the union is to commence when all unions reach an agreement. The Authority has not completed its negotiations with the pilot union to date.

Repairs and maintenance decreased 8.8%. Although the Authority continues to repair and maintain its properties, the Authority exercised care and reduced its overall cost related to repairs and maintenance in fiscal year 2012 due to the uncertainty of the economic environment in the territory and abroad.

Insurance increased by 8.3%. Insurance rates were favorable for the Authority for most policies with the exception of the property policy that increased. The addition of reverted properties during fiscal year 2012 to the Authority's property listing contributed to this increase.

Depreciation increased 3.1%. The increase resulted from new structures and equipment added during 2012.

Other operating expenses decreased 28.7%. The decrease was due to a significant set up of bad debt related to allowance for custom dues not received during fiscal year 2011 of $1.7 million and the full amount of the receivable, $3.4 million, was written off during fiscal year 2012.

In fiscal year 2011, operating expenses for the Virgin Islands Port Authority increased approximately 0.3% in comparison to a 13.7% increase in fiscal year 2010. Payroll, taxes and fringe benefits decreased by 4.6% although there were increases awarded through contractual agreements to the marine union dating back from fiscal year 2007 through fiscal year 2011. The retroactive percentages awarded were 2.75% for fiscal years 2007 through 2009, and 3% for fiscal years 2010 through 2011. Additionally, management unionized employees received salary increases of 2.25%. However the decline in payroll related expenses net of the above awards was a result of retroactive payments made to the larger population the Aviation unionized employees in fiscal year 2010 of approximately $2.6 million. The Authority continued to pay 100% of medical insurance for all employees in fiscal year 2011.

Repairs and maintenance decreased 2.4%. Although the Authority continues to repair and maintain its properties, the Authority reduced its overall cost related to repairs and maintenance in fiscal year 2011.

Insurance decreased 4.8%. Insurance rates were favorable for the Authority for most policies with the exception of the property policy which increased. The aggregate result was a decrease in the overall cost to the Authority.

Depreciation increased 7.2%. This resulted from added structures and equipment from prior years.

Other operating expenses increased 9.4%. The increase was due to increases in electrical expenses of $482 thousand, allowance for bad debt related to customer accounts of $1.3 million and allowance for custom dues not received of $1.7 million.

The following table details the components of and changes in operating expenses:

	2012	2011	2010	Change 2012	Change 2011
(In thousands of dollars)					
Payroll, payroll taxes and fringe benefits	**$ 18,300**	$ 18,595	$ 19,502	$ (295)	$ (907)
Repairs and maintenance	**3,198**	3,506	3,592	(308)	(86)
Materials, supplies and other services	**5,269**	4,889	5,721	380	(832)
Insurance	**3,582**	3,308	3,473	274	(165)
Depreciation	**20,444**	19,822	18,496	622	1,326
Other operating expenses	**7,156**	10,041	9,175	(2,885)	866
Total operating expenses	**$ 57,949**	$ 60,161	$ 59,959	$ (2,212)	$ 202

Non-Operating Revenues and Expenses

The Authority has permission from the FAA to collect passenger facilities charges ("PFC") of $4.50 for each passenger departing from CEKA and $3.00 for each passenger departing from HERA. These funds are restricted for certain capital projects as established by the Aviation Safety and Capacity Expansion Act of 1990. The Authority collected approximately $2.5 million of PFC revenues in fiscal year 2012 compared to approximately $1.5 million in fiscal year 2011. This increase can be attributed to the 82,979 increase of passenger traffic during the fiscal year, reinstitution of the PFC charges for HERA, and the increase in CEKA's PFC charges from $3.00 to $4.50.

In fiscal year 2012 the Authority recorded $4.2 million as capital assets related to five (5) leased properties that reverted to its control in what is called reversions. These improved properties are recorded based on appraised values of the site improvements that are reverting. The reverted values are shown as extraordinary income with a corresponding entry to the asset being recorded.

Capital Contributions

Capital contributions are received from the U.S. Government, mainly the Federal Aviation Administration (FAA), Federal Emergency Management Agency (FEMA), U.S. Federal Highway Administration (FHWA), Economic Development Administration (EDA), and the Government of the U.S. Virgin Islands to fund capital projects.

In fiscal year 2012 contributions amounted to $5.3 million. Federal contributions from FAA: $.3 million to rehabilitate the Cyril E. King Airport Runway, $.1 million CEKA pavement evaluation and terminal study, $1.9 million to rehabilitate the Henry E. Rohlsen Runway, $0.3 million for HERA pavement inspection, security improvement, and apron rehab. Other federal contributions came from TSA of $0.5 million for the security and canine reimbursement and $0.2 million for the HERA TSA building. U.S. Government contributions: $1.8 million for Enighed Pond cargo building.

In fiscal years 2011 and 2010, federal grants amounted to $18.5 million and $11.4 million, respectively. Federal funds received from FAA were used to rehabilitate the Cyril E. King Airport Runway, the Henry E. Rohlsen Runway (phase 1) and the balance for airport and fire rescue vehicles on St. Thomas and St. Croix; total received in 2011 - $19.6 million. Other receipts came from TSA or the security and canine reimbursement $.5 million.

Change in Net Assets

Total net assets, which represent the excess of assets over liabilities, for the Authority, decreased by $0.2 million in 2012 and increased by $4.8 million in 2011. This change resulted from total operating expenditures of $57.9 million and $60.1 million, offset by revenues of $47.2 million and $46.5 million, net non-operating revenues of $5.2 million and $(.112) million and capital contributions of $5.3 million and $18.5 million in 2012 and 2011, respectively.

Statements of Net Assets

The Statement of net assets presents the financial position of the Authority at the end of the fiscal year. A summarized comparison of the Authority's assets, liabilities and net assets at September 30, 2012, 2011, and 2010, is as follows:

	2012	2011	2010
(In thousands of dollars)			*(As restated)*
Assets			
Current assets	**$ 38,694**	$ 34,415	$ 38,385
Non-current assets:			
Capital assets, net	**240,402**	248,980	245,517
Other non-current assets	**4,792**	5,348	5,440
Total assets	**283,888**	288,743	289,342
Liabilities and Net Assets			
Liabilities:			
Current liabilities	**12,193**	14,716	18,072
Non-current liabilities - bonds payable	**28,637**	30,813	32,843
Total liabilities	**40,830**	45,529	50,915
Net assets:			
Invested in capital assets, net of related debt	**209,640**	216,144	210,735
Restricted	**10,850**	10,936	11,325
Unrestricted	**22,568**	16,134	16,367
Total net assets	**$ 243,058**	$ 243,214	$ 238,427

During fiscal year 2012, the net decrease in capital assets amounting to approximately $8.6 million was the net effect of additions to capital assets amounting to $11.8 million, net of depreciation expense of $20.4 million.

During fiscal year 2011, the net increase in capital assets amounting to $3.7 million was the net effect of additions to capital assets amounting to $23.5 million, net of depreciation expense of $19.8 million.

The most significant additions were related to the following capital projects:

	2012	2011	2010
Enighed Pond - Parking Lot	–	$1.2 million	–
Cyril E. King Fire Trucks	–	–	$.7 million
Henry E. Rohlsen Fire Trucks	–	–	$1.5 million
Enighed Pond Marine Terminal Building	**$1.8 million**	–	–
Cyril E. King Baggage Make-up Belt	**$1.5 million**	$2.9 million	–
Cyril E. King Energy System	–	$2.9 million	–
Cyril E. King Runway Roadway Lighting	–	–	$.51 million
Rehabilitate CEKA Airport Runway	–	$5.9 million	$10.2 million
HERA Runway Rehabilitation	**$1.4 million**	$6.9 million	–

Capital Financing and Debt Management

The Authority has three bond issues outstanding as of September 30, 2012. They are the 2003 Marine Revenue Series A&B Bonds and the 2003 Marine Revenue Series C Bonds.

The Marine Revenue Bonds were used to finance the dredging, rehabilitation and construction of the Crown Bay Pier in St. Thomas and the construction of a mixed used commercial complex at Crown Bay. The Marine Revenue Bonds were issued in a two part series of 2003A (AMT) and 2003B (federally taxable), in principal amounts of $18 million and $17 million.

A summary of the Marine Bonds' terms follows:

	Interest Rate
$ 5,930,000 Series A, due serially from 2015 through 2018	5.25%
$12,075,000 Series A, due serially from 2019 through 2023	5.00%
$ 6,745,000 Series B, due serially from 2003 through 2009	3.54%
$ 7,245,000 Series B, due serially from 2009 through 2013	5.08%
$ 3,435,000 Series B, due serially from 2014 through 2015	5.43%

The aggregate balance as of September 30, 2012 and 2011, for the Marine Revenue Bonds Series A&B is $23 million and $24.6 million, respectively.

In October of 2003, the Authority entered into an agreement with Banco Popular de Puerto Rico to finance the Authority's portion for the construction of the Red Hook Terminal, renovation of the Gallows Bay Dock, St. Croix and the dredging of the Crown Bay and Charlotte Amalie Harbor. This bond issuance is labeled as Marine Series C Bonds. The financing for these projects were completed on September 30, 2005 in an amount not to exceed $10.8 million. At the close of fiscal year 2012, the amount outstanding of the Marine Series C Bonds was $7.6 million.

As of September 30, 2012 and 2011, the Marine revenue bonds outstanding amounted to $30.7 million and $32.7 million, respectively, a decrease of $2.0 million compared to the balance outstanding as of September 30, 2011. The bonds outstanding as of September 30, 2012 and 2011 consisted of the Marine Revenues, series A, B and C bonds.

As discussed in Note 6 to the financial statements, both bond indentures require a debt service coverage ratio of not less than 125%. This debt service coverage is calculated based on a formula described in Note 6. In fiscal years 2012 and 2011, the Authority complied with the debt service coverage of the Bonds. The following table summarizes the results of such calculation for 2012:

Debt Service Coverage Ratio-required	125%
Fiscal year 2012 debt service coverage ratio	199%
Excess of debt service coverage over bond indentures requirement	74%

Contingencies

St. Croix Municipal Landfill at Estate Anguilla

The failure of the Government of the Virgin Islands to address the problems of the landfill and to address the fulfillment of the approved Compliance Plan between the Department of Public Works and the Federal Aviation Administration (FAA) continues to affect the Authority. The Authority is maintaining the airfields at Henry E. Rohlsen and Cyril E. King Airport mostly with federal financial assistance from FAA's Airport Improvement (AIP) Grant Program and from the discretionary funds. The AIP funds are allocated by formula or other entitlement processes. Discretionary funds are administered by the Secretary of Transportation. Since 1982, the Authority has received approximately $180 million in entitlement and discretionary funds combined. A total of $57 million in Entitlement funds and $55 million in Discretionary funds for Cyril E. King Airport, and $53 million in Entitlement funds and $15 million in Discretionary funds for Henry E. Rohlsen Airport have been received.

The FAA has decided not to accept any request for discretionary funds from the Authority until timely closure of the landfill is achieved and a long-term solution is decided. To date the solution remains pending.

Economic Factors 2012

In fiscal year 2012, the Virgin Islands Port Authority continued to encounter financial challenges resulting from the economic crises experienced in the Territory and abroad. The revenues of the Port are highly dependent on the U.S. Virgin Islands (USVI) tourism industry; in turn USVI tourism is highly dependent on the U.S. economy-particularly the availability of discretionary income. The U.S. economy, though marginally improving, is still characterized by meager growth, volatile fuel prices, and high unemployment; this translates into scarce discretionary income for travelers and-as a consequence-stagnant revenue growth for the Authority.

The present realities and outlook for the economic and tourism industry environment, in which the Authority must navigate, will require a significant focus on cost containment as an integral component of the Authority's sustainability strategy. For that reason, in 2012, the Authority installed the first of two photovoltaic solar cell arrays at its airports to reduce grid purchases of electricity. The Port will continue to implement energy efficient technologies that will further reduce its overall energy costs.

Contacting the Authority's Financial Management

This financial report is designed to provide the Authority's customers and creditors and other interested persons with a general overview of its finances and to demonstrate the Authority's accountability for the funds it receives. If you have questions about this report, or need additional financial information, contact the Director of Administration and Finance at Administrative Building, Cyril E. King Airport, St. Thomas, V.I. 00803.

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Statements of Net Assets

(In thousands of dollars)

	September 30	
	2012	**2011**
Assets		
Current assets:		
Cash and cash equivalents (restricted - $5,034 in 2012 and $4,441 in 2011)	**$ 28,881**	$ 24,461
Accounts receivable - net of allowance for doubtful accounts of $1,432 in 2012 and $2,151 in 2011	**2,997**	3,060
Short-term investments	**395**	387
Sinking funds (restricted)	**1,991**	2,213
Receivables from U.S. Government agencies	**1,157**	1,270
Receivables from the Government of the U.S.Virgin Islands, net of allowance for doubtful account of $0 in 2012 and $3,450 in 2011	**–**	145
Prepaid insurance	**2,455**	2,252
Other current assets	**818**	627
Total current assets	**38,694**	34,415
Noncurrent assets:		
Capital assets, net	**240,402**	248,980
Sinking funds (restricted)	**3,825**	4,282
Debt issue costs	**967**	1,066
Total noncurrent assets	**245,194**	254,328
Total assets	**$ 283,888**	288,743

(Continued)

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Statements of Net Assets (continued)

(In thousands of dollars)

	September 30	
	2012	**2011**
Liabilities and net assets		
Current liabilites:		
Note payable	**$ 1,929**	$ 1,515
Bonds payable	**2,125**	2,023
Accounts payable related to capital projects, including retainage on contracts	**107**	1,032
Compensated absences payable	**1,819**	1,839
Other accounts payable and accrued liabilities	**6,213**	8,307
Total current liabilities	**12,193**	14,716
Noncurrent liabilities:		
Bonds payable	**28,637**	30,813
Total liabilites	**40,830**	45,529
Net assets:		
Invested in capital assets, net of related debt	**209,640**	216,144
Restricted	**10,850**	10,936
Unrestricted	**22,568**	16,134
Total net assets	**$ 243,058**	$ 243,214

See accompanying notes.

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Statements of Revenues, Expenses and Changes in Net Assets

(In thousands of dollars)

	September 30 2012	September 30 2011
Operating revenues		
Aviation	**$ 21,379**	$ 20,468
Marine	**25,851**	26,068
	47,230	46,536
Operating expenses		
Payroll, payroll taxes and fringe benefits	**18,300**	18,595
Repairs and maintenance	**3,198**	3,506
Materials, supplies and other services	**5,269**	4,889
Insurance	**3,582**	3,308
Depreciation	**20,444**	19,822
Other operating expenses	**7,156**	10,041
Total operating expenses	**57,949**	60,161
Operating loss	**(10,719)**	(13,625)
Non-operating revenues (expenses)		
Passenger facilities charges	**2,488**	1,463
Extraordinary income	**4,200**	–
Interest income	**156**	134
Interest expense	**(1,579)**	(1,709)
Total non-operating revenues (expenses), net	**5,265**	(112)
Change in net assets before capital contributions	**(5,454)**	(13,737)
Federal and state government capital contributions	**5,298**	18,524
Change in net assets	**(156)**	4,787
Net assets at beginning of year	**243,214**	238,427
Net assets at end of year	**$ 243,058**	$ 243,214

See accompanying notes.

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Statements of Cash Flows

(In thousands of dollars)

	September 30 2012	September 30 2011
Cash flows from operating activities		
Cash received from customers and others	**$ 47,030**	$ 47,206
Cash paid to suppliers and employees, net of capitalized expenses	**(39,615)**	(41,764)
Net cash provided by operating activities	**7,415**	5,442
Cash flows from investing activities		
Proceeds (redemption) of investments	**451**	(12)
Interest received from investments	**107**	134
Net cash provided by investing activities	**558**	122
Cash flows from capital and related financing activities		
Acquisition of capital assets	**(8,590)**	(23,264)
Proceeds from note payable	**3,453**	3,173
Principal payments on bonds payable and note payable	**(5,095)**	(4,887)
Interest paid on bonds	**(1,587)**	(1,709)
Cash received from U.S. Government agencies and local government	**5,556**	19,610
Passenger facilities charges	**2,488**	1,463
Net cash used in capital and related financing activities	**(3,775)**	(5,614)
Net change in cash and cash equivalents	**4,198**	(50)
Cash and cash equivalents at beginning of year	**26,674**	26,724
Cash and cash equivalents at end of year	**$ 30,872**	$ 26,674
Cash and cash equivalents include		
Unrestricted and restriced cash and cash equivalents	**$ 28,881**	$ 24,461
Cash and cash equivalents restricted in sinking funds	**1,991**	2,213
	$ 30,872	$ 26,674

(Continued)

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Statements of Cash Flows (continued)

(In thousands of dollars)

	September 30	
	2012	**2011**
Reconciliation of operating loss to net cash provided by operating activities		
Operating loss	**$ (10,719)**	$ (13,625)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	**20,444**	19,822
Bond issuance cost amortization	**99**	99
Premium amortization	**(18)**	(18)
Provision for uncollectibles	**263**	2,382
Change in assets and liabilities:		
Accounts receivable	**(201)**	740
Receivable from the Government of the U.S. Virgin Islands	**–**	(70)
Prepaid insurance	**(203)**	(220)
Other assets	**(136)**	7
Accounts payable and other accrued liabilities	**(2,114)**	(3,675)
Total adjustments	**18,134**	19,067
Net cash provided by operating activities	**$ 7,415**	$ 5,442
Supplemental schedule of noncash investing, capital and financing activities		
Property received upon termination of leases	**$ 4,200**	$ –

See accompanying notes.

1. Reporting Entity and Summary of Significant Accounting Policies

Reporting Entity

The Virgin Islands Port Authority (the Authority) was created by Act 2375 of December 23, 1968, to operate as an autonomous agency. The Authority commenced operations on February 11, 1969, by virtue of Act 2405. The Authority owns and manages the air and marine terminals of the U.S. Virgin Islands.

The Authority is a component unit of the Government of the U.S. Virgin Islands (the Government) and, therefore, the financial statements of the Authority are not intended to present fairly the financial position and results of operations of the Government. Only the accounts of the Authority are included in the reporting entity. There are no component units that should be considered for inclusion in the Authority's financial statements.

Summary of Significant Accounting Policies

Basis of Accounting

The Authority prepares its financial statements in conformity with U.S. generally accepted accounting principles for governmental enterprise funds as prescribed by the Government Accounting Standards Board (GASB). In addition, the Authority follows all Financial Accounting Standard Board pronouncements issued prior to November 30, 1989, and certain other pronouncements subsequent to that date that do not conflict with GASB standards.

The financial statements are prepared on the accrual basis of accounting. Under this method revenues are recorded when earned and expenses recorded at the time liabilities are incurred.

Basic Financial Statements

Standards for external financial reporting for state and local governments require that resources be classified for accounting and reporting purposes into net assets categories and to report the changes in net assets. Net assets represent the residual interest in the Authority's assets after liabilities are deducted and consist of the following categories:

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Summary of Significant Accounting Policies (continued)

Basic Financial Statements (continued)

- *Invested in capital assets, net of related debt:* Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets. The portion of debt attributed to the unspent debt proceeds is included in the same net asset component as the unspent proceeds.

- *Restricted:* These result when constraints, on the use of net assets, are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

- *Unrestricted:* Net assets that are not subject to externally imposed stipulations.

The Authority distinguishes operating revenues and expenses from non-operating items. Operation revenues and expenses generally result from providing services in connection with the Authority's principal ongoing operations. The principal operating revenues of the Authority are charges to customers for fees, dues and rent on each air and marine terminal. Operating expenses for the Authority include the cost of services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

Sources of Income

The Authority derives most of its income from user fees and rental charges. These amounts are charged to the users of its airports, harbors and terminal facilities at St. Thomas, St. Croix and St. John and recorded as operating revenues. The Authority is empowered by law to establish and charge the necessary fees and dues to permit the recovery of facility costs.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Passenger Facilities Charges (PFCs)

The airlines that use the Authority's airport facilities collect a Passenger Facility Charge (PFC) of up to $4.50 per passenger from travelers leaving the U.S. Virgin Islands. As approved by the Federal Aviation Administration (FAA), the use of funds generated by the PFC is restricted for the construction of certain FAA approved capital projects. The PFCs, less an administrative fee charged by the airlines for processing, are collected by the airlines and remitted on a monthly basis to the Authority. The Authority recognizes the revenues when it receives the PFCs collected by airlines. Due to their restricted use, PFCs are categorized as non-operating revenues and are recorded as restricted net assets until the funds are expended. Once funds generated by PFCs are used in the construction of the FAA approved projects, such amounts are transferred to net assets invested in capital assets, net of related debt.

Grants and Contributions from Federal and State Government Grants

The Authority receives federal and state government grants mainly to support its capital construction program. The assets and revenues arising from government grants are recorded when the Authority meets the eligibility requirements. Grants for capital projects are reported as other revenues. If resources are received in advance of satisfying certain eligibility requirements, the recognition of revenues is deferred.

Cash Equivalents

The Authority considers non-negotiable certificates of deposit and highly-liquid investments with a maturity of three months or less when purchased, excluding those in sinking funds accounts, to be cash equivalents in the accompanying statements of net assets. For purposes of the statements of cash flows, cash and cash equivalents also include the current portion of restricted balances deposited in the sinking funds.

Accounts Receivable

Accounts receivable are recorded at their gross value when earned and are reduced by the estimated portion that is expected to be uncollectible. The adequacy of the allowance for doubtful accounts is evaluated by management based upon past collection experience and customers' financial condition.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Investments

Investments are recorded at fair value in the statements of net assets and report changes in their fair value in the statements of revenues, expenses and changes in net assets as non-operating revenue or expense. Fair value of investments is based on quoted market prices. Short-term investments, which consist of non-negotiable certificates of deposits and other highly liquid investments such as U.S. Government and agencies securities with a maturity of less than one year when purchased, are carried at amortized cost, which approximates fair value due to their short term maturities.

The Authority maintains certain investments deposited in sinking funds that are restricted for specific uses in accordance with the corresponding bond indentures. These investments are presented in the statements of net assets within the sinking fund balances (see Note 3).

Interest

Interest on funds used to finance construction of qualifying projects is capitalized unless it has been funded with internally generated funds or government grants limited for use in such projects. Capitalized interest expense is reduced by interest income earned on related investments acquired with proceeds of tax exempt borrowings. During 2012 and 2011, no interest expense was capitalized.

Capital Assets

Land transferred from the Federal Government or from the Government of the U.S. Virgin Islands is carried at the Government's original cost if the information is available; if not, it is carried at amounts estimated by management to approximate cost at the time the properties were acquired by the U.S. Virgin Islands from the Federal Government. Depreciable assets transferred at inception by the Government of the U.S. Virgin Islands are carried at amounts estimated based on total capital expenditures incurred by predecessor agencies. Depreciation has been accumulated on such assets from the dates the predecessor agencies incurred the expenditures and placed the assets in operation, based on their estimated average life. All other capital assets are carried at cost.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Capital Assets (continued)

Depreciation is calculated using the straight-line method over the estimated useful lives of the individual assets. Estimated useful lives of capital assets are as follows:

	Years
Buildings and structures	20 - 40
Runways, aprons and pavings	10
Equipment	5 - 10
Land and harbor improvements	20

When assets are retired, the cost and related accumulated depreciation of the property is removed from the accounts and any gain or loss is recognized as non-operating revenue or expense. Expenditures for major renewals and betterments are capitalized, while maintenance and repairs which do not extend the life of the assets are recorded as expenses.

Debt Issue Costs and Original Bond Issue Premium

Bond and notes premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the debt. Bonds and notes payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported separately on the statement of net assets and amortized over the term of the related debt.

Compensated Absences

Unpaid vacation leave compensation, as well as the Authority's share of related social security taxes, are accrued as benefits are earned by the employees if attributable to past services and if it is probable the Authority will compensate the employees for such benefits. Amounts accrued are measured using salary rates in effect at September 30.

Pension Plan

The Authority follows the provisions of GASB Statement No. 27. Under this statement, the pension expense is equal to the statutory required contribution to the plan. See Note 10 for further discussion.

1. Reporting Entity and Summary of Significant Accounting Policies (continued)

Fair Values of Financial Instruments

The Authority uses the following methods and assumptions in estimating its fair value disclosures:

Investment securities held in sinking funds are valued at quoted market prices when available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments or from values obtained from independent pricing sources.

The carrying amounts of cash and cash equivalents, money market investments, accounts receivable and other receivables, accounts payable and other accrued liabilities approximate their fair values given the short-term nature of the instruments.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make 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 reporting period. Actual results could differ from those estimates.

2. Cash and Cash Equivalents

Cash and cash equivalents, segregated by category at September 30, 2012 and 2011, are as follows (in thousands of dollars):

	2012		2011	
	Bank Balance	**Carrying Amount**	**Bank Balance**	**Carrying Amount**
Restricted	**$ 5,025**	**$ 5,034**	$ 4,441	$ 4,441
Unrestricted	**24,536**	**23,847**	21,709	20,020
	$ 29,561	**$ 28,881**	$ 26,150	$ 24,461

2. Cash and Cash Equivalents (continued)

At September 30, 2012 and 2011, restricted cash and cash equivalents consisted of PFC's deposited in interest bearing accounts. Unrestricted cash and cash equivalents may be used for operational purposes.

As of September 30, 2012, approximately $22 million or 75.8% of the Authority's deposits in banks were held at Banco Popular de Puerto Rico.

As of September 30, 2011, approximately $16.0 million or 65.5% of the Authority's deposits in banks were held at Banco Popular de Puerto Rico.

3. Sinking Funds and Short-Term Investments

The amounts deposited in the sinking funds are restricted for specific uses in accordance with the corresponding bond indentures, mainly for construction and maintenance of airports and marine facilities. The bond indentures also require the Authority to maintain certain balances to cover the bonds debt service reserves (see Note 6). The Authority is not permitted to use these funds for any other purpose.

Investments in the reserve accounts at September 30, 2012, were as follows (in thousands of dollars):

	2012		
	2003 Series A & B Marine Revenue Bonds	**2003 Series C Marine Revenue Bonds**	**Total**
Restricted:			
Debt service reserve	**$ 3,824**	**$ 868**	**$ 4,692**
Construction	**9**	**10**	**19**
Operating maintenance renewal and replacement funds	**1,103**	**1**	**1,105**
	$ 4,936	**$ 879**	**$ 5,816**

3. Sinking Funds and Short-Term Investments (continued)

Investments in the reserve accounts at September 30, 2011, were as follows (in thousands of dollars):

	2011		
	2003 Series A & B Marine Revenue Bonds	2003 Series C Marine Revenue Bonds	Total
Restricted:			
Debt service reserve	$ 4,512	$ 863	$ 5,375
Construction	9	10	19
Operating maintenance renewal and replacement funds	1,100	1	1,101
	$ 5,621	$ 874	$ 6,495

Restricted investments, categorized by investment type, and weighted average maturity, for 2012 and 2011, are as follows (in thousands of dollars):

	2012		2011	
	Fair Value	Weighted Avg. Maturity (Years)	Fair Value	Weighted Avg. Maturity (Years)
Cash and cash equivalents and deposits	**$ 5,816**	**3.98**	$ 6,495	3.84

3. Sinking Funds and Short-Term Investments (continued)

Interest Rate Risk

Interest rate risk represents the exposure to fair value losses arising from increasing interest rates. The Authority does not have a formal investment policy that limits investment maturities as a means of managing such exposure.

Credit Risk

The authorizing legislation of the Authority does not limit investments by credit rating categories. Authorizing legislation limits the investment choices of the Authority to: direct obligations or obligations guaranteed by the United States, obligations of states, territories, possessions and commonwealths of the United States, obligations of international banking institutions, repurchase agreements, investment contracts, certificates of deposits, guaranteed investment contracts, shares in mutual funds and, investment companies, corporate commercial paper, money market accounts and investment pools.

Concentration of Credit Risk

The Authority places no limit on the amount that may be invested in one issuer. At September 30, 2012, 76% of the Authority's sinking funds and short-term investments were invested in US Bank U.S.A. The composition of sinking funds and short-term investments are as follows: cash and cash equivalents accounts (76%), BPPR time deposit account (1.8%), and certificates of deposits (6%).

At September 30, 2011, 83% of the Authority's sinking funds and short-term investments were invested in HSBC Bank U.S.A. The composition of sinking funds and short-term investments are as follows: cash and cash equivalents accounts (78%), BPPR time deposit account (16%), and certificates of deposits (6%).

3. Sinking Funds and Short-Term Investments (continued)

Custodial Credit Risk

The Authority does not have a custodial risk policy. This is the risk that the Government will not be able to recover the value of its investments that are in the possession of an outside party. At September 30, 2012, all investments of the Authority were held in the name of US Bank USA, N.A., as Trustee for the Authority. Investments in the trust accounts are limited to the investments permitted by the trust indenture.

4. Capital Assets

Capital assets as of September 30, 2012, comprise as follows:

(In thousands of dollars)	2011	Increase	Decrease	Transfers	2012
Capital assets not being depreciated:					
Land	$ 20,696	$ –	$ –	$ –	**$ 20,696**
Construction in progress	14,366	6,975	–	(15,901)	**5,440**
Total capital assets not being depreciated	35,062	6,975	–	(15,901)	**26,136**
Capital assets being depreciated:					
Buildings and structures	307,522	4,200	–	2,565	**314,287**
Runways, aprons and pavings	140,693	12	–	7,634	**148,339**
Equipment	29,103	654	–	4,865	**34,622**
Land and harbor improvements	26,932	–	–	837	**27,769**
Total capital assets being depreciated	504,250	4,866	–	15,901	**525,017**
Accumulated depreciation for:					
Buildings and structures	(148,029)	(9,396)	–	–	**(157,425)**
Runways, aprons and pavings	(101,577)	(7,268)	–	–	**(108,845)**
Equipment	(16,067)	(1,892)	–	–	**(17,959)**
Land and harbor improvements	(24,659)	(1,863)	–	–	**(26,522)**
Total accumulated depreciation	(290,332)	(20,419)	–	–	**(310,751)**
Total capital assets, net	$ 248,980	$ (8,578)	$ –	$ –	**$ 240,402**

4. Capital Assets (Continued)

Capital assets as of September 30, 2011, as restated, comprise as follows:

(In thousands of dollars)	2010	Increase	Decrease	Transfers	2011
Capital assets not being depreciated:					
Land	$ 20,696	$ –	$ –	$ –	$ 20,696
Construction in progress	2,502	22,448	(178)	(10,406)	14,366
Total capital assets not being depreciated	23,198	22,448	(178)	(10,406)	35,062
Capital assets being depreciated:					
Buildings and structures	307,476	36	–	10	307,522
Runways, aprons and pavings	133,474	–	–	7,219	140,693
Equipment	25,067	859	–	3,177	29,103
Land and harbor improvements	26,813	119	–	–	26,932
Total capital assets being depreciated	492,830	1,014	–	10,406	504,250
Accumulated depreciation for:					
Buildings and structures	(138,644)	(9,385)	–	–	(148,029)
Runways, aprons and pavings	(94,924)	(6,653)	–	–	(101,577)
Equipment	(14,347)	(1,720)	–	–	(16,067)
Land and harbor improvements	(22,596)	(2,063)	–	–	(24,659)
Total accumulated depreciation	(270,511)	(19,821)	–	–	(290,332)
Total capital assets, net	$ 245,517	$ 3,641	$ (178)	$ –	$ 248,980

5. Notes Payable

In 2012, the Authority borrowed approximately $3.5 million to finance certain insurance premiums. The notes payable bear interest at 3.1% and 3.49% and are payable in monthly installments over periods not exceeding 11 months. The balance outstanding as of September 30, 2012 was approximately $1.9 million.

5. Notes Payable (continued)

In 2011, the Authority borrowed approximately $3.2 million to finance certain insurance premiums. The notes payable bear interest at 3.1% and 2.75% and are payable in monthly installments over periods not exceeding 11 months. The balance outstanding as of September 30, 2011 was approximately $1.5 million.

Changes in notes payable for the years ended September 30, 2012 and 2011 follow (in thousands of dollars):

	2011	Increase	Decrease	2012
Insurance loan at 3.10%	$ 1,315	**$ 2,997**	**$ (2,627)**	**$ 1,685**
Insurance loan at 3.49%	–	**456**	**(212)**	**244**
Insurance loan at 2.75%	200	**–**	**(200)**	**–**
	$ 1,515	**$ 3,453**	**$ (3,039)**	**$ 1,929**

	2010	Increase	Decrease	2011
Insurance loan at 3.10%	$ 1,085	$ 2,726	$ (2,496)	$ 1,315
Insurance loan at 3.49%	216	–	(216)	–
Insurance loan at 2.75%	–	447	(248)	200
	$ 1,301	$ 3,173	$ (2,959)	$ 1,515

6. Bonds Payable

At September 30, 2012 and 2011, bonds payable consist of:

(In thousands of dollars)	**2012**	2011
Marine Division:		
2003 Marine Revenue Bonds, $18,005 Series A; due serially from September 1, 2005, through September 1, 2023, bearing interest ranging from 5.00% to 5.25%	**$ 18,005**	$ 18,005
2003 Marine Revenue Bonds, $17,425 Series B; due serially through September 1, 2015, bearing interest ranging from 3.73% to 5.43%	**5,035**	6,555
2003 Marine Revenue Draw Bonds, up to $10,750 Series C; due serially through September 1, 2023, bearing interest of 4.40%	**7,634**	8,171
	30,674	32,731
Debt premium	**88**	105
Less current portion of long-term debt	**(2,125)**	(2,023)
	$ 28,637	$ 30,813

The aggregate debt service requirements of bonds payable at September 30, 2012, follow:

(In thousands of dollards) **Years**	**Principal**	**Interest**	**Total**
2013	$ 2,125	$ 1,506	$ 3,631
2014	2,228	1,400	3,628
2015	2,347	1,283	3,630
2016	2,467	1,162	3,629
2017	2,588	1,036	3,624
2018 through 2022	15,035	3,106	18,141
2023 through 2024	3,884	199	4,083
Total	$ 30,674	$ 9,692	$ 40,366

6. Bonds Payable (continued)

Changes in bonds payable for the years ended September 30, 2012 and 2011, follow:

(In thousands of dollars)	2011	Increase	Decrease	2012
2003 Series A Marine Revenue Bonds	$ 18,005	**$ –**	**$ –**	**$ 18,005**
2003 Series B Marine Revenue Bonds	6,555	**–**	**(1,520)**	**5,035**
2003 Series C Marine Revenue Bonds	8,171	**–**	**(537)**	**7,634**
Premium and debt issue costs	105	**–**	**(17)**	**88**
	$ 32,836	**$ –**	**$ (2,074)**	**$ 30,762**

(In thousands of dollars)	2010	Increase	Decrease	2011
2003 Series A Marine Revenue Bonds	$ 18,005	$ –	$ –	$ 18,005
2003 Series B Marine Revenue Bonds	8,000	–	(1,445)	6,555
2003 Series C Marine Revenue Bonds	8,654	–	(483)	8,171
Premium and debt issue costs	123	–	(18)	105
	$ 34,782	$ –	$ (1,946)	$ 32,836

The Marine Revenue Bonds do not constitute general obligations of the Authority, the Aviation Division, the Marine Division, the U.S. Virgin Islands or the United States of America.

On January 16, 2003, the Authority issued the Marine Revenue Bonds Series 2003A (AMT) and 2003B (federally taxable), with principal amounting to approximately $18 million and $17.4 million, respectively. The Authority used the proceeds of the bonds to finance dredging, rehabilitation and construction of berthing piers for cruise and seagoing vessels at Crown Bay in St. Thomas, and the construction of a mixed used commercial facility.

On October 20, 2003, the Authority issued the Marine Revenue Bonds Series 2003C (Non-AMT), with an authorized principal amount not to exceed approximately $10.8 million. The Authority used the proceeds of the bonds to finance the completion of several projects to include rehabilitation and construction of berthing piers for cruise and seagoing vessels at Crown Bay in St. Thomas, and the construction at Red Hook, Enighed Pond, Gallows Bay Dock, and dredging of the Charlotte Amalie Harbor.

6. Bonds Payable (continued)

Neither the credit of the U.S. Virgin Islands nor that of its political subdivisions is pledged or available for the payment of principal or interest on the bonds.

The bonds indentures contain certain account restrictions and funding covenants to cover interest, debt service, maintenance and other costs specified in the corresponding bond indentures. Management believes that the Authority has established the aforementioned required accounts and has complied with the contribution requirements with respect to the bonds. In addition, it is management's opinion that the Authority has complied with limitations and restrictions imposed by the bond indentures.

The bonds indentures also specify certain debt service coverage requirements determined from Net Available Revenues (as defined) of the Authority's Marine Division. The provisions of each of the bonds indentures require that rates and fees charged for the use of each facility generate enough revenues to pay all operation and maintenance expenses, exclusive of depreciation and certain non-cash charges, of the respective facilities plus (a) at least 125% of the principal and interest, and redemption account sinking fund deposit requirements of each of the bonds becoming due during such year, (b) the amount of the debt service reserve fund deposit requirement for such period, (c) the deposit required to the Renewal and Replacement Fund, and (d) the amount of the capital improvements appropriation for such period.

For fiscal year 2012, the Authority did not comply with the requirement to issue the audited financial statements within 150 days after year-end. However, as per the Authority's bond indenture, this noncompliance event does not constitute an event of default until the Trustee sends a notification of failure and such failure continues for 90 days. The Authority did receive notification from its Trustee but noncompliance was covered within the 90 days.

7. User Agreements and Leases

The Authority has entered into long-term user agreements and leases with several air carriers for use of the Airport System facilities. Under the terms of the user agreements and leases, the air carriers have agreed to pay airfield landing fees in CEKA and HERA, and terminal, concourse, hangar, cargo, and maintenance facility rentals and certain miscellaneous charges in consideration for use of the CEKA facilities. The user agreements and leases also require the Authority to make certain capital improvements and to provide maintenance of certain airport facilities. There are no such long-term use agreements covering the HERA terminal.

7. User Agreements and Leases (continued)

The Authority is required under the agreements with the airlines to estimate its maintenance and operation costs and revenues for the next fiscal year and to furnish such estimate to the airlines. In the event that the actual maintenance and operation costs for the year are greater than the amount estimated for that period, the deficit has to be added to the estimate of such costs to be incurred in the succeeding year, and if the actual maintenance and operation costs for the year are less than the amount estimated, the surplus amount has to be deducted from the estimate to be incurred in the succeeding year.

The user rates are revised annually and are determined in consultation with the Authority's independent rate consultants. Effective October 1, 2005, the Authority adjusted its rate after the HERA bonds were paid off. The Authority ceased the signatory and non-signatory differentiation in rate and instituted one user fee for all carriers at $2.50 per 1,000 pounds.

8. Contributions to/from the Government of the U.S. Virgin Islands

In June 2002, the Authority contributed $4 million to the Government of the U.S. Virgin Islands. The Authority agreed to make such contribution to receive in return $18.5 million from the Virgin Islands Public Finance Authority, another component unit of the Government of the U.S. Virgin Islands, in future years. The funds to be received will be used in the development of two capital projects of the marine division. The Authority will receive the funds on a reimbursement basis as allowable costs are incurred. In order to be entitled to receive such funds, the projects must meet the requirements of the federal agencies and the Authority is obligated to spend the grant moneys in accordance with the regulatory restrictions. During 2007, the Authority received approximately $2.5 million from the Virgin Island Public Finance Authority to develop the capital projects. These amounts were recorded as government grants in the Statement of Revenues, Expenses and Changes in Net Assets.

9. Related Party Transactions

During the fiscal years ended September 30, 2012 and 2011, another enterprise fund of the Government of the U.S. Virgin Islands charged the Authority approximately $6.8 million and $6.7 million, respectively, for utility services rendered. Charges for such services are recurring and are included in the Authority's operating expenses. During Fiscal year 2012 the Authority also paid Department of Planning and Natural Resources fees for submerged land rentals of approximately $.3 million and this entity also paid the authority $.45 million in office rental fees.

10. Pension Plan

Substantially all of the Authority's employees are covered by the Employee Retirement System of the Government of the U.S. Virgin Islands (the System), a cost-sharing multiple-employer defined benefit pension plan. The System is a public employee retirement plan sponsored by the Government of the U.S. Virgin Islands that was created by Act No. 479, approved on June 24, 1959. The System became operative on October 1, 1959, at which date contributions by employees and the Government commenced. Substantially all full-time employees of the Government and its related agencies are covered by the System.

The System provides for retirement, death and disability benefits for employees and their dependents. The administrator of the System is responsible for its proper operation, subject to orders, resolutions and directives of a Board of Trustees. The governor of the U.S. Virgin Islands, with the approval of the Legislature, could change the required contributions from the employers and employees. Although the Government has not expressed any intent to terminate the Plan, it may do so at any time. In the event of termination of the Plan, the rights of all affected participants and beneficiaries to whom benefits have accrued under the Plan shall be non-forfeitable to the extent funded.

Government and members contributions are set by statute. The Government's required contribution remained the same as Fiscal Year 2008 at the contribution rate of 17.5% and required member contributions remained unchanged at 8% of the annual salary for regular employees entering service before 1/1/2011 and 8.5% for regular employees entering service from 1/1/2011, 9% for senators and 10% or 10.5% for certain employees covered by Act 5226 based on the date they entered service. The Government's contributions, together with the members' contributions and the income of the System should theoretically be sufficient to provide adequate actuarially determined reserves to cover the payment of the annuities and benefits provided by the System. The latest actuarial valuation indicates that the current combined statutory employer and employee contribution rates are not sufficient to meet the cost of the System on an actuarial reserve, as required by law. The System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained from the System's Administrator. The Authority's contributions for the years ended September 30, 2012 and 2011 were approximately $2 million for each of the years.

11. Risk Management

The Authority is exposed to various risks of losses, including torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority obtains coverage, among others, for up to a maximum of $1 million for each general liability claim, and $45 million for each property liability claim. The property liability policy imposes several deductibles not exceeding $250,000 under any event. The Authority is also covered by terrorism property and liability policies with coverage of $45 million.

Claims expenditures and liabilities are recorded when it is probable that a loss has occurred in excess of insured amounts and the amount of that loss can be reasonably estimated. The Authority suffered a loss due to fire of one of its properties in fiscal year 2012. The loss on the property has not been reasonable determined as of the end of the fiscal year.

12. Contingencies

In connection with federal and state governments grant programs, the Authority is obligated to administer and spend the grant monies in accordance with regulatory restrictions, and is subject to audit by the grantor agencies. In cases of non-compliance, the agencies involved may require the Authority to refund program monies. Management believes these non-compliance instances, if any, should not materially affect the Authority's financial position.

The Federal Aviation Administration (FAA) conducted an onsite wildlife evaluation of the landfill, airport and surrounding area of the Anguilla Landfill at St. Croix. The landfill, that is adjacent to St. Croix airport (Henry E. Rohlsen), caused environmental and navigational problems to the airport. The landfill attracts flocks of birds and there have been plane crashes elsewhere when birds have flown into jet engines. The FAA is threatening to force the Authority, to repay $9.3 million in grants previously awarded and to refuse further grants for the airport unless the Authority and the USVI Government show rapid progress toward closing the landfill.

The landfill is under the jurisdiction of another agency of the Government. Thus, the Government and the Authority proposed a remediation plan to operate the landfill and close it by December 2009. FAA accepted the plan, if such measures are implemented. The Authority's management believes that the plan is being implemented and complied with as agreed with the FAA. Under the remediation plan, the Authority is responsible for the maintenance of the surrounding areas to reduce the risk that flocks of birds cause a plane crash and repossess adjacent miscellaneous properties.

12. Contingencies (continued)

During the normal course of business, the Authority is a defendant in various lawsuits. In the opinion of management and legal counsel, the outcome of these cases and resulting liability, if any, is either adequately covered by insurance or should not materially affect the Authority's financial position.

13. Lease Agreements

The Authority leases several properties within its Aviation and Marine Divisions to outside users under the terms of numerous lease agreements. Leased facilities within the Aviation Division include warehouse areas at the airports, counter space within the terminals, and retail space for terminal concessionaires. The Marine Division leases warehouse, commercial and office space within the Crown Bay pier area to outside users as well.

The lease agreements at September 30, 2012 and 2011, include contracts with non-cancelable terms for both fixed and variable rental charges. The agreements expire at various dates through 2017. During fiscal year 2012 and 2011, the Authority generated revenues of approximately $9.8 million and $9.9 million, respectively, through the leasing arrangements. Future estimated minimum fixed rentals under non-cancelable lease agreements and month-to-month follow:

Year Ending September 30,	Amount
2013	$ 10,668,024
2014	11,074,344
2015	11,219,859
2016	11,379,584
2017	11,340,908
	$ 55,682,718

14. Credit Concentration

The Authority's revenues are dependent on a small group of air-carriers and shipping lines. Its revenues are particularly affected by demand fluctuations affecting the tourism industry, in particular tourism from the east coast of the United States.

In fiscal years 2012 and 2011, the following customers provided more than 10% of the Aviation and Marine Divisions' total operating revenues as follows:

	Division	2012	2011
American Airlines	Aviation	**20.4%**	**17.9%**
Carnival Cruise Line	Marine	**12.7%**	**10.6%**
Princess Cruises	Marine	**-**	**10.5%**
Royal Caribbean Cruise Lines	Marine	**21.0%**	**19.3%**

15. Significant New Accounting Pronouncements

Future Adoption of Accounting Standards

GASB has issued the following accounting standards that the Authority has not yet adopted:

GASB Statement		Adoption required in fiscal year
	Arrangements	
61	Accounting and Financial Reporting Entity: Omnibus-an amendment of GASB Statements No. 14 and No. 34	2013
62	Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements	2013
63	Financial Reporting of Deferred Outflows of Resources, Deferred Inflows od Resources, and Net Position	2013
64	Derivative Instruments: Application of Hedge Accounting Termination Provisions - an amendment of GASB Statement No. 53	2012
65	Items previously reported as Assets and Liabilities	2013
66	Technical corrections - 2012 an amendment of GASB Statements No. 10 and 62	2013
70	Accounting and Financial Reporting for Nonexchange Financial Guarantees	2014

The impact of these standards has not yet been determined.

Other Financial Information
(Unaudited)

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Schedule of Revenues and Expenses – Aviation Division (Unaudited)

Years Ended September 30, 2012 and 2011

(In thousands of dollars)

	St. Thomas Airport	Special Facilities	St. Croix Airport	2012 Total	2011 Total
Operating revenues					
Users' fees and dues	$ 9,705	$ –	$ 2,814	**$ 12,519**	$ 12,116
Rentals	3,369	516	1,085	**4,970**	4,867
Others	3,069	149	672	**3,890**	3,485
Total operating revenues	16,143	665	4,571	**21,379**	20,468
Operating expenses					
Payroll, payroll taxes and fringe benefis	2,867	–	2,403	**5,270**	4,536
Repairs and maintenance	1,278	134	515	**1,927**	1,910
Materials, supplies and other services	809	3	475	**1,287**	1,230
Insurance	1,107	5	549	**1,661**	1,512
Depreciation	7,726	–	4,789	**12,515**	11,748
Other operating expenses	3,340	(17)	1,766	**5,089**	4,805
General and administrative allocation	4,394	32	2,693	**7,119**	6,430
Total operating expenses	21,521	157	13,190	**34,868**	32,171
Operating (loss) income	(5,378)	508	(8,619)	**(13,489)**	(11,703)
Non-operating revenues(expenses):					
Passenger facilities charges	1,982	–	506	**2,488**	1,462
Extraordinary income	–	1,384	2,676	**4,060**	–
Interest income	35	5	–	**40**	63
Interest expense	(18)	–	(2)	**(20)**	(15)
Total non-operating revenues, net	1,999	1,389	3,180	**6,568**	1,510
Change in net assets before capital contributions	(3,379)	1,897	(5,439)	**(6,921)**	(10,193)
Federal and state government grants	952	–	2,579	**3,531**	17,054
Change in net assets	$ (2,427)	$ 1,897	$ (2,860)	**$ (3,390)**	$ 6,861

See accompanying notes to other financial information.

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Schedule of Revenues and Expenses – Marine Division (Unaudited)

Years Ended September 30, 2012 and 2011

(In thousands of dollars)

	St. Thomas Airport	Special Facilities	St. Croix Airport	2011 Total
Operating revenues				
Users' fees and dues	$ 13,192	$ 872	**$ 14,064**	$ 14,483
Wharfage dues	4,916	1,000	**5,916**	5,590
Rentals	4,429	424	**4,853**	5,019
Others	948	70	**1,018**	976
Total operating revenues	23,485	2,366	**25,851**	26,068
Operating expenses				
Payroll, payroll taxes and fringe benefits	3,606	1,170	**4,776**	5,269
Repairs and maintenance	465	136	**601**	1,061
Materials, supplies and other services	1,493	660	**2,153**	2,023
Insurance	1,192	515	**1,707**	1,591
Depreciation	5,184	2,364	**7,548**	7,707
Other operating expenses	1,331	246	**1,577**	4,749
General and administrative allocation	3,405	1,306	**4,711**	5,595
Total operating expenses	16,676	6,397	**23,073**	27,995
Operating income (loss)	6,809	(4,031)	**2,778**	(1,927)
Non-operating revenues (expenses):				
Extraordinary income	140	–	**140**	–
Interest income	87	16	**103**	71
Interest expense	(1,554)	–	**(1,554)**	(1,689)
Total non-operating revenues (expenses),net	(1,327)	16	**(1,311)**	(1,618)
Change in net assets before capital contributions	5,482	(4,015)	**1,467**	(3,545)
Federal and state government grants	1,767	–	**1,767**	1,470
Change in net assets	$ 7,249	$ (4,015)	**$ 3,234**	$ (2,075)

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Schedule of General and Administrative Expenses (Unaudited)

Years Ended September 30, 2012 and 2011

(In thousands of dollars)

	2012	2011
Payroll, payroll taxes and fringe benefits	**$ 8,254**	$ 8,790
Repairs and maintenance	**669**	535
Material, supplies and other services	**1,830**	1,636
Insurance	**214**	205
Depreciation	**381**	367
Other operating expenses	**490**	487
Interest expense	**(8)**	5
	$ 11,830	$ 12,025
Allocated as follows:		
Aviation	**$ 7,119**	$ 6,430
Marine	**4,711**	5,595
	$ 11,830	$ 12,025

See accompanying notes to other financial information.

Virgin Islands Port Authority
(A Component Unit of the Government of the U.S. Virgin Islands)

Schedule of Net Available Revenues for the Marine Division (Unaudited)

Years Ended September 30, 2012 and 2011

(In thousands of dollars)

	2012	2011
Revenues		
Operating revenues:		
Users' fees and dues	**$ 19,980**	$ 20,073
Rentals	**4,853**	5,019
Others	**1,018**	977
Interest income	**103**	71
Total revenues	**25,954**	26,140
Expenses		
Operating expenses:		
Payroll, payroll taxes and fringe benefits	**4,776**	5,269
Repairs and maintenance	**601**	1,061
Materials, supplies and other services	**2,153**	2,023
Insurance	**1,707**	1,591
Other operating expenses	**1,577**	4,749
General and administrative allocation	**4,711**	5,595
Total expenses	**15,525**	20,288
Net available revenues	**$ 10,429**	$ 5,852

See accompanying notes to other financial information.

Notes to Other Financial Information (Unaudited)

September 30, 2012 and 2011

1. Description of Schedules

The Schedules of Revenues and Expenses present the revenues and expenses of the Aviation Division and the Marine Division, respectively.

The Schedules of Net Available Revenues, as defined in the Bonds' Indentures, excludes all depreciation and certain non-cash charges. This schedule also excludes PFC revenue and government grants, which are not available for payment of debt service because they are restricted for the construction of certain capital projects approved by the federal and local governments.

2. General and Administrative Expenses

For purposes of this presentation and consistent with the Authority's financial practices, an allocation of general and administrative expenses is made to each of the divisions. Such expenses include depreciation and maintenance related to administrative divisions. These allocations are calculated on the basis of other operating expenses, excluding depreciation.

Other Report

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Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Directors
Virgin Islands Port Authority

We have audited the financial statements of the Virgin Islands Port Authority (the Authority), a component unit of the Government of the U.S. Virgin Islands, as of and for the years ended September 30, 2012 and 2011, and have issued our report thereon dated July 8, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

Management of the Authority is responsible for establishing and maintaining effective internal controls over financial reporting. In planning and performing our audit, we considered the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weakness as defined below.

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

A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. .

Compliance and Other Matters

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

This report is intended solely for the information and use of Management, Audit Committee, Board of Directors, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

July 8, 2013

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