

**BORDER ENVIRONMENT
COOPERATION COMMISSION**

Financial Statements

December 31, 2015 and 2014

(With Independent Auditors' Report Thereon)



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Independent Auditors' Report

(Translation from Spanish Language Original)

The Board of Directors
Border Environment Cooperation Commission

We have audited the accompanying financial statements of Border Environment Cooperation Commission (the "Commission"), which comprise the statements of financial position as of December 31, 2015 and 2014, and the statements of activities and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Mexican Financial Reporting Standards (FRS), and for such internal control as Management determines is necessary to enable the preparation 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 audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, we consider 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of 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.

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Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Border Environment Cooperation Commission as of December 31, 2015 and 2014, and its statements of activities and cash flows for the years then ended, in accordance with Mexican Financial Reporting Standards.

Emphasis of Matter

As mentioned in note 1, the Commission was incorporated in 1993 as a result of an agreement between the governments of the United States of America and Mexico. The Commission was created with the purpose of helping preserve, protect and enhance the environment in the border region common to both countries. The Commission is funded through annual budgeted federal contributions from both countries as well as contributions from the United States Environmental Protection Agency (“EPA”), and by the North American Development Bank. The Commission possesses the legal status of organization of public international law.

KPMG CARDENAS ROSAL, S. C.

A handwritten signature in black ink, appearing to read 'Guillermo Cutierrez Frias', is written over a large, loopy scribble. The signature is positioned above the printed name 'Guillermo Cutierrez Frias'.

Guillermo Cutierrez Frias

April 1st, 2016

BORDER ENVIRONMENT COOPERATION COMMISSION

Statements of Financial Position

December 31, 2015 and 2014

(U. S. dollars)

	<u>2015</u>	<u>2014</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 5,334,912	3,518,246
Recoverable value-added tax	72,930	33,519
Other accounts receivable	17,867	11,151
Prepaid expenses	3,135	9,912
Contributions receivable (note 4)	<u>2,052,773</u>	<u>4,742,245</u>
Total current assets	7,481,617	8,315,073
Contributions receivable (note 4)	6,910,002	7,111,562
Machinery, furniture and equipment, net (note 5)	95,403	155,545
Intangible assets, net (note 6)	<u>78,201</u>	<u>138,003</u>
	<u>\$ 14,565,223</u>	<u>15,720,183</u>
Liabilities and Fund Balance		
Current liabilities:		
Accrued expenses (note 7)	\$ <u>2,464,485</u>	<u>445,527</u>
Total current liabilities	2,464,485	445,527
Employee benefits (note 8)	<u>19,721</u>	<u>19,721</u>
Total liabilities	<u>2,484,206</u>	<u>465,248</u>
Fund balance:		
Unrestricted fund balance (note 9)	<u>12,081,017</u>	<u>15,254,935</u>
Total fund balance	12,081,017	15,254,935
Commitment and contingent liabilities	_____	_____
	<u>\$ 14,565,223</u>	<u>15,720,183</u>

See accompanying notes to financial statements

BORDER ENVIRONMENT COOPERATION COMMISSION

Statements of Activities

Years ended December 31, 2015 and 2014

(U. S. dollars)

	<u>2015</u>	<u>2014</u>
Changes in unrestricted fund balance:		
Contributions – Department of State (DOS)	\$ 2,373,000	2,386,000
Contributions – Mexico-Secretariat of Environment and Natural Resources (SEMARNAT)	1,792,650	1,793,750
Contributions - United States of America- Environmental Protection Agency	647,252	785,500
Contributions - North American Development Bank	<u>725,000</u>	<u>600,000</u>
	<u>5,537,902</u>	<u>5,565,250</u>
Administrative expenses and project related costs:		
Salaries and benefits	4,161,446	4,034,768
Travel and transportation expenses	378,064	401,565
Public events	149,729	305,380
Technical assistance and fees	2,879,475	3,500,369
Other expenses	<u>1,154,019</u>	<u>1,087,205</u>
	<u>8,722,733</u>	<u>9,329,287</u>
Interest income, net	<u>10,913</u>	<u>13,158</u>
Decrease in unrestricted fund balance	(3,173,918)	(3,750,879)
Unrestricted fund balance at beginning of year	<u>15,254,935</u>	<u>19,005,814</u>
Unrestricted fund balance at end of year	<u>\$ 12,081,017</u>	<u>15,254,935</u>

See accompanying notes to financial statements

BORDER ENVIRONMENT COOPERATION COMMISSION

Statements of Cash Flows

Years ended December 31, 2015 and 2014

(U. S. dollars)

	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:		
Decrease in unrestricted fund balance	\$ (3,173,918)	(3,750,879)
Items relating to investing activities:		
Depreciation	89,812	21,094
Amortization	<u>59,802</u>	<u>46,000</u>
Subtotal	<u>(3,024,304)</u>	<u>(3,683,785)</u>
Contributions receivable	2,891,032	3,644,163
Recoverable value-added tax	(39,411)	6,160
Other accounts receivable	(6,716)	10,672
Prepaid expenses	6,777	(1,982)
Accrued expenses	<u>2,018,958</u>	<u>198,821</u>
Net cash provided by operating activities	<u>1,846,336</u>	<u>174,049</u>
Cash flows from investing activities:		
Acquisition of machinery, furniture and equipment and net cash used in investing activities	<u>(29,670)</u>	<u>(15,626)</u>
Net increase in cash and cash equivalents	1,816,666	158,423
Cash and cash equivalents:		
At beginning of year	<u>3,518,246</u>	<u>3,359,823</u>
At end of year	<u>\$ 5,334,912</u>	<u>3,518,246</u>

See accompanying notes to financial statements

BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

December 31, 2015 and 2014

(U. S. dollars)

The financial statements have been translated from the Spanish language original and for the convenience of English-speaking readers.

(1) Description of the Commission Activity:

The Border Environment Cooperation Commission (the “Commission”) was incorporated in 1993 as a result of an agreement between the governments of the United States of America and Mexico. The Commission was created with the purpose of helping preserve, protect and enhance the environment in the border region common to both countries. The Commission is funded through annual budgeted federal contributions from both countries as well as contributions from the United States Environmental Protection Agency (“EPA”), and by the North American Development Bank. The Commission possesses the legal status of organization of public international law.

The property, other assets, income and operations of the Commission are exempt from any responsibility related to payment, withholding and taxes or contributions in Mexico and the United States, based on the agreement between the government of Mexico and the United States of America. The agreement provides that for the fulfillment of its purpose and functions, the Commission shall enjoy in the territory of each of the parties the status, immunities and privileges in this agreement published in the Mexican Federal Official Gazette (DOF) in 1993, and subsequently amended in 2004.

(2) Financial statement authorization and presentation:

Authorization

On April 1st, 2016, Ms. Gloria Melendez, Commission’s Administrative Director authorized the issuance of the accompanying financial statements and related notes thereto.

Basis of preparation

a) Statement of compliance

The accompanying financial statements of the Commission have been prepared in accordance with Mexican Financial Reporting Standards (FRS).

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BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

(U. S. dollars)

b) Use of estimates and judgments

The preparation of financial statements requires Management to make a number of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of machinery, furniture and equipment, intangible assets and assets and liabilities related to employee benefits. Actual results could differ from those estimates and assumptions.

c) Functional and reporting currency

The aforementioned financial statements are presented in US dollars, which is the same as the local currency and the functional currency.

(3) Summary of significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, and have been applied consistently by the Commission:

a) Cash and cash equivalents-

Cash and cash equivalents consist of checking accounts, foreign currency and other highly liquid instruments. At the date of the financial statements, interest income is included in the statements of activities.

b) Machinery, furniture and equipment-

The machinery, furniture and equipment are recorded at acquisition cost.

The depreciation on machinery, furniture and equipment is calculated on the straight-line method, over the estimated useful lives of the assets as determined by the Commission's Management. The total useful lives of the principal asset classes are as follows:

	<u>Years</u>
Transportation equipment	5
Furniture and equipment	10
Computer equipment	3
Machinery and equipment	2

Minor repairs and maintenance costs are expensed as incurred.

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BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

(U. S. dollars)

c) Intangible assets-

Intangible assets with a definite useful life include mainly computer software and computer systems. These assets are recorded at acquisition or development cost and amortized using the straight line over their estimated useful life of three years.

d) Accruals-

Based on Management's estimates, the Commission recognizes accruals for present obligations where the transfer of assets or the rendering of services is virtually inevitable and arises as a consequence of past events, principally employee salary and benefits.

e) Employee benefits-

Since the Commission has the legal status of organization of public international law, the relation between the Commission and its employees occurs by individual labor contracts that establish the benefits granted to the employees.

In the case of seniority premium provisions, employees make contributions to individual retirement funds, established in an agreement between the Commission and the employees.

Employee benefits consist of a seniority premium for which the Commission has a provision based on estimates by Management. The severance payment consists of a one-time payment of three months' wages which are expensed as incurred.

f) Contributions recognition-

Contributions received are recognized according to the annual budget commitment by the federal governments of Mexico and the United States of America, as well as by the U.S. Environmental Protection Agency ("EPA"), and beginning in 2012 by the North American Development Bank.

The contributions received by the Commission are established from the moment of its constitution and represent an annual variation in the fund balance of \$1,792,650 and \$1,793,750 as of December 31, 2015 and 2014, respectively, that is contributed by the Government of Mexico and \$2,373,000 and \$2,386,000, that is contributed by the United States Government. The Commission also receives contributions from the EPA and from the North American Development Bank based on authorized projects.

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BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

(U. S. dollars)

g) Contingencies-

Liabilities for important loss contingencies are recorded when it is probable that a liability has been incurred and the amount thereof can be reasonably estimated. When a reasonable estimation cannot be made, disclosure is provided in the notes to the financial statements.

(4) Contributions receivable:

The main contributions receivables to EPA consist of the following:

<u>Grant name</u>	<u>Grant number</u>	<u>2015</u>	<u>2014</u>
<u>Short term:</u>			
B2012 R9	X400T6270	\$ 732,188	1,114,175
PDAP R9	XP00T2960	1,139,897	1,604,839
Others	Several	<u>180,688</u>	<u>2,023,231</u>
Total		\$ <u>2,052,773</u>	<u>4,742,245</u>
<u>Long term:</u>			
B2012 R6	X400F5950	\$ 332,945	-
B2020 R6	X400F9250	324,047	-
B2020 R6	X401F0490	434,524	-
B2020 R9	X499T0660	549,171	-
B2020 R9	X499T2800	434,461	-
PDAP R6	XP9669760	2,125,032	2,278,252
PDAP R6	XP9666470	1,830,939	2,967,160
PDAP R9	XP00T6740	878,883	1,035,279
PDAP R9	XP9893830	-	314,171
Others	Several	<u>-</u>	<u>516,700</u>
Total		\$ <u>6,910,002</u>	<u>7,111,562</u>

These contributions are used for certification of projects for the conservation, protection and improvement of the environment in the border region between Mexico and the United States of America. The application of these contributions initiated by requests made by states, municipalities and other entities public and private investors for certification of projects, for which the applicant seeks to obtain financial assistance from the Development Bank of North America or other sources of financing.

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BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

(U. S. dollars)

Contributions receivable, short-term, they are considered those whose recovery is expected within a period not exceeding one year after the date of the statement of the financial position.

(5) Machinery, furniture and equipment:

The machinery, furniture and equipment comprise the following:

	<u>2015</u>	<u>2014</u>
Transportation equipment	\$ 94,071	94,071
Furniture and equipment	257,540	246,659
Computer equipment	225,286	239,123
Machinery and equipment	<u>82,828</u>	<u>82,828</u>
	659,725	662,681
Less:		
Accumulated depreciation	<u>564,322</u>	<u>507,136</u>
	<u>\$ 95,403</u>	<u>155,545</u>

The building in which the Commission's offices are located, is provided by the Mexican Federal Government at no cost to the Commission. The Commission leases another building from a private party to accommodate additional parking and conference rooms.

(6) Intangible assets:

Intangible assets as of December 31, 2015 and 2014, are as follows:

	<u>2015</u>	<u>2014</u>
Software	\$ 184,003	184,003
Accumulated amortization	<u>105,802</u>	<u>46,000</u>
	<u>\$ 78,201</u>	<u>138,003</u>

(7) Accrued expenses:

The accrued expenses include liabilities for goods or services incurred at year end, as well as accrued vacations to be paid. The balance of accrued expenses at December 31 2015 and 2014, amounted to \$2,464,485 and \$445,527, respectively.

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BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

(U. S. dollars)

(8) Employee benefits:

Consists of payments to which employees are entitled to under their contracts, equivalent to a maximum of three months base salary for termination without cause. For such purposes, the Commission has a provision determined based on estimates by the Commission Management. The liability amounted to \$19,721 at December 31, 2015 and 2014.

(9) Unrestricted fund balance:

The unrestricted fund balance consist of federal contributions by the United States of America Environmental Protection Agency (EPA), less cost and expenses incurred in providing services for certification of projects aimed at environmental conservation, protection and improvements in the border area between Mexico and the United States of America, and performing Commission's management activities.

At December 31, 2015 and 2014, the restricted fund balance is a present below:

<u>Contributions</u>	<u>2015</u>	<u>2014</u>
Authorized	\$ 23,896,517	49,884,436
Applied	<u>(15,122,947)</u>	<u>(38,452,654)</u>
Pending application	8,773,570	11,431,782
Commission's results	<u>3,307,447</u>	<u>3,823,153</u>
Unrestricted fund balance	<u>\$ 12,081,017</u>	<u>15,254,935</u>

(10) Commitment and contingent liabilities:

a) The Commission has a lease contract for a building it uses for various purposes, that expires on April 4, 2016. The contract would be renewed for up to 2 more years.

Total rent expenses, for the years ended December 31, 2015 and 2014, amounted to \$37,525 and \$42,457, respectively. Total rents payable under this agreement is as follows:

2016	<u>\$ 13,645</u>
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b) There is a contingent liability arising from the employee benefits mentioned in note 3(e).

c) The commission has obligations to consultants in accordance with project progress.

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BORDER ENVIRONMENT COOPERATION COMMISSION

Notes to Financial Statements

(U. S. dollars)

(11) Recently issued financial reporting standards:

The Mexican Board of Financial Information Standards has issued the FRS and Improvements listed below:

2016 FRS Improvements

In December 2015, CINIF issued the document referred to as “2016 FRS Improvements”, which contains precise modifications to some FRS. The modifications that bring about accounting changes are listed below:

FRS C-1 “Cash and cash equivalents” and FRS B -2 “Statement of cash flows”-These modify the definition of cash and cash equivalents to make consistent with the definitions established in the International Financial Reporting Standards (IFRS) and changes the term “investments available on demand” to “highly-liquid financial instruments”. It also stipulates that cash on the initial and subsequent recognition should be valued at fair value, which is face value, cash equivalents should be valued at fair value on initial recognition and highly-liquid financial instruments should be valued based in the provisions of the standard for financial instruments, in accordance with the purpose for which each type of instrument is maintained. These revisions are effective for years beginning on or after January 1, 2016 and the accounting changes that arise should be recognized retrospectively.

Management estimates that the new FRS and the improvements to FRS will be immaterial.