Audited Financial Statements
AES Puerto Rico Limited Partnership
As of and for the years ended December 31, 2017 and 2016
with Report of Independent Auditors

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Contents

AES Puerto Rico Limited Partnership
Balance Sheets
December 31, 2017 and 2016
(In Thousands of U.S. Dollars)

	Notes	2017	2016
		(in thousands)	
ASSETS			
CURRENT ASSETS			
Cash	2	$ **21,259**	$ 22,827
Restricted cash and debt reserves	2	**38,373**	24,067
Accounts receivable, net of allowance for doubtful accounts of $275	2	**83,977**	83,981
Receivable from affiliates	4	**331**	319
Inventory, net	5	**27,101**	26,921
Prepaid expenses		**1,451**	1,086
Other current assets		**45**	488
Total current assets		**172,537**	159,689
NONCURRENT ASSETS			
Property, Plant and Equipment:			
Land	6	**5,074**	5,074
Electric generation assets and others (including spare parts of $5,717 and $4,885, respectively)	2, 6	**795,946**	791,406
Accumulated depreciation	6	**(255,318)**	(237,911)
Construction in progress	6	**2,473**	4,299
Property, plant and equipment, net		**548,175**	562,868
Other Assets:			
Restricted cash — noncurrent	2	**–**	25,946
Other intangible assets, net of accumulated amortization of $1,900 and $1,859, respectively	2, 7	**87**	122
Prepaid expenses - noncurrent		**3,128**	2,931
Total other assets		**3,215**	28,999
TOTAL ASSETS		$ **723,927**	$ 751,556

See accompanying notes to the audited financial statements.

AES Puerto Rico Limited Partnership
Balance Sheets
December 31, 2017 and 2016
(In Thousands of U.S. Dollars)

	Notes	2017	2016
		(in thousands)	
LIABILITIES AND PARTNERS' EQUITY			
CURRENT LIABILITIES			
Accounts payable and accrued liabilities		**$ 12,144**	$ 39,032
Payable to affiliates	4	**9,784**	8,537
Long-term debt — current, net of debt discount of $6,050 and net of deferred financing costs of $3,126	2, 8	**365,474**	77,199
Derivative liability — current	9	**–**	857
Income tax payable	13	**1,195**	2,522
Other current liabilities		**1,681**	1,685
Total current liabilities		**390,278**	129,832
LONG-TERM LIABILITIES			
Long-term debt - noncurrent	2, 8	**–**	332,911
Deferred revenue — noncurrent	2	**105,685**	89,284
Deferred income taxes — noncurrent	13	**16,024**	15,965
Other long-term liabilities		**187**	91
Total long-term liabilities		**121,896**	438,251
PARTNERS' EQUITY			
Partners' contributions	12	**37,287**	37,164
Retained earnings		**177,724**	151,076
Accumulated other comprehensive loss- net of taxes of $1,070 and $1,133, respectively		**(3,258)**	(4,767)
Total partners' equity		**211,753**	183,473
TOTAL LIABILITIES AND PARTNERS' EQUITY		**$ 723,927**	$ 751,556

See accompanying notes to the audited financial statements.

1. General

AES Puerto Rico Limited Partnership (the "Partnership") was formed in 1994 as a limited partnership under the laws of the State of Delaware. AES Puerto Rico, Inc., the general partner, owns a 1% interest in the Partnership and AES Monroe Holdings, BV, the limited partner, owns the remaining 99% of the Partnership. Both, AES Puerto Rico, Inc. and AES Monroe Holdings, BV, are indirect wholly owned subsidiaries of The AES Corporation ("AES").

The Partnership was formed for the purpose of developing, constructing, owning, and operating a cogeneration facility (the "Plant") in Guayama, Puerto Rico. The Plant consists of a power plant and a marine terminal. The power plant, a coal-fired electric facility, has a design capacity for the generation of 454.3 net megawatts ("MW") of electricity for sale to Puerto Rico Electric Power Authority ("PREPA") under a 25-year Power Purchase and Operating Agreement ("PPA") from the commercial operating date, November 29, 2002. The marine terminal consists of a dock, a pier and associated structures, and an enclosed, reversible conveyor belt connecting the marine terminal to the Plant for the unloading of coal and limestone and loading of ash.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of these financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") requires the Partnership to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most important estimates are the useful lives of long-lived assets and the assessments of potential disputes and claims.

Fair Value

Fair value, as defined in ASC 820, *"Fair Value Measurement"*, is the price that would be received to sell an asset or paid to transfer a liability in an orderly, hypothetical transaction between market participants at the measurement date, or exit price. The Partnership applies the fair value measurement accounting guidance to financial assets and liabilities in determining the fair value of derivative liabilities.

The Partnership applies the fair value measurement guidance to nonfinancial liabilities in conjunction with the measurement of an impairment loss on an asset group under the accounting guidance for the impairment of long-lived assets.

2. Summary of Significant Accounting Policies (continued)

The fair value measurement accounting guidance requires that the Partnership makes assumptions that market participants would use in pricing an asset or liability based on the best information available. These factors include nonperformance risk (the risk that the obligation will not be fulfilled) and credit risk of the reporting entity (for liabilities) and of the counterparty (for assets).

The fair value measurement guidance prohibits the inclusion of transaction costs and any adjustments for blockage factors in determining the instruments' fair value. The principal or most advantageous market should be considered from the perspective of the reporting entity.

Fair value is based on observable quoted market prices where available. Where they are not available, specific valuation models and techniques are applied depending on what is being fair valued. These models and techniques maximize the use of observable inputs and minimize the use of unobservable inputs. The process involves varying levels of management judgment, the degree of which is dependent on price transparency and complexity. An asset's or liability's level within the fair value hierarchy is based on the lowest level of input significant to the fair value measurement, where Level 1 is the highest and Level 3 is the lowest. The three levels are defined as follows:

Level 1—Unadjusted quoted prices in active markets accessible by the reporting entity for identical assets or liabilities. Active markets are those in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2—Pricing inputs other than quoted market prices included in Level 1 which are based on observable market data, that are directly or indirectly observable for substantially the full term of the asset or liability. These include quoted market prices for similar assets or liabilities, quoted market prices for identical or similar assets in markets that are not active, adjusted quoted market prices, inputs from observable data such as interest rate and yield curves, volatilities or default rates observable at commonly quoted intervals or inputs derived from observable market data by correlation or other means.

Level 3—Pricing inputs that are unobservable or less observable, from objective sources. Unobservable inputs are only used to the extent observable inputs are not available. These inputs maintain the concept of an exit price from the perspective of a market participant and reflect assumptions of other market participants. The Partnership considers all market participant assumptions that are available without unreasonable cost and effort. These are given the lowest priority and are generally used in internally developed methodologies to generate management's best estimate of the fair value when no observable market data is available.

2. Summary of Significant Accounting Policies (continued)

The fair value of long-lived assets determined using a discounted cash flows valuation models for impairment evaluation purposes qualify as Level 3. Any transfers between all levels within the fair value hierarchy levels are recognized at the end of the reporting period.

The Partnership's derivatives qualify as Level 2 and consist of interest rate swaps. Additional discussion regarding the nature of these financial instruments and valuation techniques for derivatives can be found in *Note 9 - Derivatives*. Any transfers between all levels within the fair value hierarchy levels are recognized at the end of the reporting period.

Cash

The Partnership considers unrestricted cash on hand, deposits in banks, certificates of deposit, and short-term marketable securities, that mature within three months or less from the date of purchase, to be cash and cash equivalents.

Restricted Cash and Debt Reserves

Restricted cash and debt reserves include cash balances which are restricted as to withdrawal or usage. The nature of restrictions includes restrictions imposed by the financing agreements, such as debt service reserves, maintenance reserves, and others.

The balance for restricted cash and debt reserves in current assets was $38.4 million and $24.1 million as of December 31, 2017 and 2016, respectively. As per the security deposit agreement, these balances constitute security for the next payment and performance by the Partnership of the long term debt, and shall at all times be subject to the sole dominion and control of the institution that holds the collateral on behalf of the lenders, and shall be held in the custody in trust for the purposes of, and on the terms set forth in, the loan agreement.

There was no balance in restricted cash noncurrent relating to debt service reserves as of December 31, 2017, the reason is explained in Note 3. The balance in restricted cash noncurrent relating to debt service reserves was $25.9 million as of December 31, 2016. In connection with its credit agreement, the Partnership is required to maintain debt service reserves for debt service payments and maintenance reserves for the payment of costs associated with the repair and replacement of capital equipment necessary for the operation of the plant and it shall be holds in the term of the loans.

Interest on the reserves is reported in interest income. Amounts in these accounts that would otherwise be considered cash and cash equivalents are treated as noncurrent assets due to their restricted use.

2. Summary of Significant Accounting Policies (continued)

Allowance for Doubtful Accounts

The Partnership reviews its accounts receivable for collectibility and records an allowance for doubtful accounts for estimated uncollectible accounts receivable. Accounts receivable are written off when they are no longer deemed collectible. Write-offs would be deducted from the allowance and subsequent recoveries would be added. The allowance is based on the Partnership's assessment of known delinquent accounts, historical experience and other currently available evidence of the collectibility and the aging of accounts receivable. The underlying assumptions, estimates and assessments the Partnership uses to provide for losses are updated to reflect the Partnership's view of current conditions. Changes in such estimates could significantly affect the allowance for losses.

The balance of allowance for doubtful as of December 31, 2017 and 2016 was $0.3 million.

Inventory

Inventory consists of coal and aragonite used to generate electricity, and spare parts and supplies used to maintain electric generation assets and others. Inventory is carried at lower of cost or market. Cost is determined under the first-in, first-out ("FIFO") method for coal and aragonite and average cost method for spare parts and supplies. Generally, cost is reduced to market value if the market value of inventory has declined and it is probable that the benefit of inventory, in its disposal in the ordinary course of business, will not be recovered through revenue earned from the generation of electricity.

Derivatives and Hedging Activities

Derivatives consist of interest rate swaps. The Partnership uses derivative instruments to manage its interest rate exposure. The Partnership does not enter into derivative transactions for trading purposes.

Under the accounting standards for derivatives and hedging, the Partnership recognizes all contracts that meet the definition of a derivative, except those designated as normal purchase or normal sale at inception, as either assets or liabilities in the Balance Sheets and measures those instruments at fair value. Changes in the fair value of derivatives are recognized in earnings unless specific hedge criteria are met. Gains and losses related to derivative instruments that qualify as hedges are recognized in the same category as generated by the underlying asset or liability. Gains or losses on derivatives that do not qualify for hedge accounting are recognized as interest expense for interest rate derivatives. ASC 815, *"Accounting for Derivative Instruments and Hedgings Activities"*, enable companies to designate qualifying derivatives as hedging instruments based on the exposure being hedged. These hedge designations include fair value hedges and cash flow hedges.

2. Summary of Significant Accounting Policies (continued)

Changes in the fair value of a derivative designated as highly effective that qualifies as a fair value hedge are recognized in earnings as offsets to the changes in fair value of the exposure being hedged. The Partnership has no fair value hedges at this time. Changes in the fair value of a derivative designated as highly effective that qualifies as a cash flow hedge are deferred in accumulated other comprehensive loss and are recognized into earnings as the hedged transactions affect earnings. Any ineffectiveness is recognized in earnings immediately. The ineffective portion is recognized as interest expense for interest rate hedges. For all hedge contracts, the Partnership maintains formal documentation of the hedge and effectiveness testing in accordance with the accounting standards for derivatives and hedging. If the Partnership determines that the derivative is not highly effective as a hedge, hedge accounting will be discontinued prospectively.

For cash flow hedges of forecasted transactions, the Partnership estimates the future cash flows of the forecasted transactions and evaluates the probability of the occurrence and timing of such transactions. Changes in conditions or the occurrence of unforeseen events could require discontinuance of hedge accounting or could affect the timing of the reclassification of gains or losses on cash flow hedges from accumulated other comprehensive loss into earnings.

The Partnership has elected not to offset net derivative positions in the financial statements. Accordingly, the Partnership does not offset such derivative positions against the fair value of amounts (or amounts that approximate fair value) recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) under master netting arrangements.

See *Note 14—Fair Value* and the Partnership's fair value policy for additional discussion regarding the determination of the fair value of the Partnership's derivative liabilities.

Income Taxes

The Partnership's income tax rate was 4% as of December 31, 2017 and 2016. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. These items are stated at the enacted tax rates that are expected to be in effect when taxes are actually paid or recovered.

Property, Plant and Equipment

Property, plant and equipment are stated at cost, net of accumulated depreciation. The costs of renewals and improvements that extend the useful life of property, plant, and equipment are capitalized.

2. Summary of Significant Accounting Policies (continued)

Construction progress payments, engineering costs, insurance costs, salaries, interest, and other costs directly relating to construction in progress are capitalized during the construction period, provided the completion of the project is deemed probable, or expensed at the time the Partnership determines that development of a particular project is no longer probable. The continued capitalization of such costs is subject to ongoing risks related to successful completion, including those related to government approvals, site identification, financing, construction permitting and contract compliance. Construction in progress balances are transferred to electric generation assets and others when each asset is ready for its intended use.

Depreciation, after consideration of residual value, is computed using the straight-line method over the estimated useful lives of the assets, which are determined on a composite or component basis. Maintenance and repairs are charged to expense as incurred if expenditures do not meet the criteria for capitalization, including costs in connection with planned major maintenance activities.

The residual value of the depreciable assets, the estimated useful lives and the depreciation methods are reviewed by management, and adjusted at the end of the year when deemed necessary. The estimated useful lives are as follows:

Generation equipment	30 years
Buildings	30 years
Office, furniture and other equipment	12 years

An item of property plant and equipment and any other significant part initially recognized is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statements of comprehensive income when the asset is derecognized.

Capital spare parts, including rotable spare parts, are included in electric generation assets and others. If the part is considered a component, it is depreciated over its useful life after the part is placed in service. If the part is deemed part of a composite asset, the part is depreciated over the composite asset life. Vehicles are depreciated under the component method.

Impairment of Long-Lived Assets

The Partnership evaluates the impairment of long-lived assets using internal projections of undiscounted cash flows when circumstances indicate that the carrying amount of such assets may not be recoverable. The carrying amount of a long-lived asset (asset group) may not be recoverable if it exceeds the sum of undiscounted cash flows expected to result from the use and eventual disposal of the asset.

2. Summary of Significant Accounting Policies (continued)

In such cases, fair value of the long-lived asset is determined in accordance with the fair value measurement accounting guidance. The excess of carrying amount over fair value, if any, is recognized as an impairment expense. No such impairments were identified or recorded in 2017 and 2016.

Intangible Assets

Intangible assets acquired separately are initially recorded at cost. Subsequent to its initial recognition, intangible assets are accounted for at cost less accumulated amortization and the accumulated amount of any impairment loss as applicable.

Deferred Financing Costs and Debt Discount

Costs incurred in connection with the issuance of long-term debt are deferred and amortized over the life of the long-term debt ranging from 17 to 26 years. Costs paid to third parties related to debt issuances are considered deferred financing costs and amortized using the effective interest method; costs paid to a lender are viewed as a debt discount and amortized using the straight line amortization method. Amortization under this method does not differ materially from the effective interest method. Total amortization expense was $1.3 million for the years ended December 31, 2017 and 2016, and is included in the statements of comprehensive income as a component of interest expense.

Revenue Recognition

The Partnership generates energy revenues under the PPA under the term of the 25-year year agreement. The revenues include: energy payment consisting of a pass through of fuel cost, capacity payment representing capital recovery and return on investment and fixed and variable operation and maintenance component payment as well as ancillary services.

Revenues from the sales of electric energy are calculated and recorded based on output delivered at rates as specified under contract terms. Revenues for fixed and variable and maintenance component variable operation and maintenance component including ancillary are recorded when the services are rendered. The Partnership determined that revenue capacity payments should be recorded in accordance with ASC 840-10-25, *"Leases Recognition"*, due to changes in contract terms of the PPA that resulted from the Settlement Agreement executed on April 5, 2011.

Under ASC 840-10-25, the arrangement does contain a lease, which was operating in nature, and the capacity payments should be recognized on a straight-line basis and all other revenue streams would be recorded as contingent rentals over the remaining term of the arrangement.

(In Thousands of U.S. Dollars)

2. Summary of Significant Accounting Policies (continued)

At December 31, 2017, future minimum capacity payments under the PPA are as follow:

Years ending December 31:		
2018	$	124,651
2019		124,651
2020		124,651
2021		124,651
2022		124,651
Thereafter		602,478
Total	$	1,225,733

Deferred Revenue

Through the PPA, generation assets of the Partnership are explicitly mentioned and it is not economically feasible or practicable for it to perform its obligation through other sources; based on that criterion, the PPA was concluded to be an operating lease. The demand charge portion plus the approximately $16.5 million in deferred revenue was accounted for as a part of the minimum lease payment and will be recognized on a straight-line basis over the remaining term of the PPA as an operating lease. The balance for deferred revenue in long term liabilities was $105.7 million and $89.3 million as of December 31, 2017 and 2016, respectively.

New Accounting Pronouncements

The following table provides a brief description of recent accounting pronouncements that had and/or could have a material impact on the Partnership's financial statements. Accounting pronouncements not listed below were assessed and determined to be either not applicable or are expected to have no material impact on the Partnership's financial statements.

New Accounting Standards Adopted

ASU Number and Name	Description	Date of Adoption	Effect on the financial statements upon adoption
2016-09, Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting	The standard simplifies the following aspects of accounting for share-based payments awards: accounting for income taxes, classification of excess tax benefits on the statement of cash flows, forfeitures, statutory tax withholding requirements, classification of awards as either equity or liabilities and classification of employee taxes paid on statement of cash flows when an employer withholds shares for tax-withholding purposes. Transition method: The recognition of excess tax benefits and tax deficiencies arising from vesting or settlement were applied retrospectively. The elimination of the requirement that excess tax benefits be realized before they are recognized was adopted on a modified retrospective basis.	January 1, 2017	The recognition of excess tax benefits in the provision for income taxes in the period when the awards vest or are settled, rather than in paid-in-capital in the period when the excess tax benefits are realized, resulted in a decrease of deferred tax liabilities, offset by an increase to retained earnings.

(In Thousands of U.S. Dollars)

2. Summary of Significant Accounting Policies (continued)

New Accounting Standards Issued But Not Yet Effective

ASU Number and Name	Description	Date of Adoption	Effect on the financial statements upon adoption
2017-12, Derivatives and Hedging (Topic 815): Targeted improvements to Accounting for Hedging Activities	The standard updates the hedge accounting model to expand the ability to hedge nonfinancial and financial risk components, reduce complexity, and ease certain documentation and assessment requirements. When facts and circumstances are the same as at the previous quantitative test, a subsequent quantitative effectiveness test is not required. The standard also eliminates the requirement to separately measure and report hedge ineffectiveness. For cash flow hedges, this means that the entire change in the fair value of a hedging instrument will be recorded in other comprehensive income and amounts deferred will be reclassified to earnings in the same income statement line as the hedged item. Transition method: modified retrospective with the cumulative effect adjustment recorded to the opening balance of retained earnings as of the initial application date. Prospective for presentation and disclosures.	January 1, 2019. Early adoption is permitted.	The Partnership is currently evaluating the impact of adopting the standard on its financial statements.
2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force)	This standard requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. Transition method: retrospective.	January 1, 2018. Early adoption is permitted.	The Partnership is currently evaluating the impact of adopting the standard on its financial statements.
2016-02, 2018-01, Leases (Topic 842)	ASU 2016-02 and its subsequent corresponding updates require lessees to recognize assets and liabilities for most leases but recognize expenses in a manner similar to today's accounting. For Lessors, the guidance modifies the lease classification criteria and the accounting for sales-type and direct financing leases. The guidance also eliminates today's real estate-specific provisions. The standard must be adopted using a modified retrospective approach at the beginning of the earliest comparative period presented in the financial statements (January 1, 2017). The FASB proposed amending the standard to give another option for transition. The proposed transition method would allow entities to not apply the new lease standard in the comparative periods presented in their financial statements in the year of adoption. Under the proposed transition method, the entity would apply the transition provisions on January 1, 2019 (i.e., the effective date). At transition, lesses and lessors are permitted to make an election to apply a package of practical expedients that allow them not to reassess: (1) whether any expired or existing contracts are or contain leases, (2) lease classification for any expired or existing leases, and (3) whether initial direct costs for any expired or existing leases qualify for capitalization under ASC 842. These three practical expedients must be elected as a package and must be consistently applied to all leases. Furthermore, entities are also permitted to make an election to use hindsight when determining lease term and lessees can elect to use hindsight when assessing the impairment of right-of-use assets. Under ASC 842, it is expected that fewer contracts will contain a lease. However, due to the elimination of today's real estate-specific guidance and changes to certain lessor classification criteria, more leases will qualify as sales-type leases and direct financing leases.	January 1, 2019. Early adoption is permitted.	The Partnership is currently evaluating the impact of adopting the standard on its financial statements and intends to adopt the standard as of January 1, 2019.

(In Thousands of U.S. Dollars)

2. Summary of Significant Accounting Policies (continued)

2014-09, 2015-14, 2016-08, 2016-10, 2016-12, 2016-20, 2017-13, Revenue from Contracts with Customers (Topic 606)	ASU 2014-09 and its subsequent corresponding updates provides the principles an entity must apply to measure and recognize revenue. The core principle is that an entity shall recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Amendments to the standard were issued that provide further clarification of the principle and to provide certain transition expedients. The standard will replace most existing revenue recognition guidance in GAAP. The standard requires retrospective application and allows either a full retrospective adoption in which all of the periods are presented under the new standard or a modified retrospective approach in which the cumulative effect of initially applying the guidance is recognized at the date of initial application. In 2016, the Partnership established a cross-functional implementation team and is in the process of evaluating changes to our business processes, systems and controls to support recognition and disclosure under the new standard. At the time of this financial statements, is not expected any significant impact on the financial systems or a material change to controls as a result of the implementation of the new revenue recognition standard.	January 1, 2018. Early adoption is permitted only as of January 1, 2017.	The Partnership adopted the standard on January 1, 2018.

3. Concentration of Risk

The main risks associated with the Partnership's financial instruments are credit risk, market risk, liquidity risk and cash flow risk.

Credit risk - Represents the potential loss from the failure of counterparties to meet their payment obligations.

Market risk - The Partnership is also exposed to changes in interest rates. In order to reduce its financial costs, the Partnership uses derivative financial instruments as hedges against identified risks.

Financial instruments which potentially subject the Partnership to concentrations of credit risk are cash and cash equivalents, trade accounts receivable and derivative financial instruments. The Partnership's policy is designed to avoid limit its exposure to one financial institution. The Partnership uses derivatives, and these agreements carry the risk that the counterparty may be unable to meet in full its obligations which could give rise to a material loss.

Liquidity risk - PREPA is the Partnership's sole customer. PREPA's payments under the PPA are expected to provide all of the Partnership's revenues and cash flows during the term of the PPA. It is uncertain whether the Partnership would be able to find another purchaser of power on similar terms for the Partnership's facility if PREPA were not performing under the PPA. Any material failure by PREPA to make capacity payments under the PPA would have a material adverse impact on the Partnership's operations.

3. Concentration of Risk (continued)

Cash flow risk - Since the Partnership depends on PREPA for revenues under the PPA, if PREPA were to terminate or default under the PPA, there would be a material adverse impact on the Partnership's cash flow and financial condition that could result in a default on its senior secured bonds.

Due to variability in power prices, if the Partnership were required to seek alternatives as a result of a default by PREPA, any such alternate revenues might be substantially below the amounts that would have been otherwise payable pursuant to the PPA. There can be no assurance as to the Partnership's ability to generate sufficient cash flow to cover operating expenses or its debt service obligations in the absence of a long-term PPA with PREPA.

Concentration of Credit Risk

The Partnership is exposed to concentrations of credit risk primarily related to cash, restricted cash and account receivable. The Partnership mitigates its exposure to credit risk by maintaining deposits at highly rated financial institutions and by monitoring the credit quality of the related financial institution and counterparties of the Partnership's contracts. The Partnership's operations are concentrated within Puerto Rico, and any changes to government policies for renewable energy, including revisions or changes to renewable energy tax legislation, could have a negative effect on the Partnership's activities, financial condition, and results of operations.

Known and unknown risks, uncertainties and other factors outside the Partnership control may cause actual results to differ materially from its current expectations. These risks, uncertainties and factors include but are not limited to risks and uncertainties related to the financial condition and continued performance of the third parties on which the Partnership depends, including Puerto Rico Electric Power Authority (PREPA), the possibility of unexpected problems related to the performance of the facility, the possibility of unexpected expenses or lower-than-expected revenues and additional factors that are unknown to the Partnership or beyond its control.

The Partnership have long term PPAs with state-owned PREPA which has been facing challenges that could impact the Partnership.

In order to address these challenges, on June 30, 2016, the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA") was signed into law. PROMESA created a structure for exercising federal oversight over the fiscal affairs of U.S. territories and allowed for the establishment of an Oversight Board with broad powers of budgetary and financial control over Puerto Rico. PROMESA also created procedures for adjusting debts accumulated by the Puerto Rico government and, potentially, other territories ("Title III"). Finally, PROMESA expedites the approval of key energy projects and other critical projects in Puerto Rico.

3. Concentration of Risk (continued)

PREPA entered into preliminary Restructuring Support Agreements ("RSAs") with their lenders. Under PROMESA, PREPA submitted the RSA to the Oversight Board for approval on April 28, 2017, which the board denied on June 28, 2017. As a consequence, on July 2, 2017, the Oversight Board filed for bankruptcy on behalf of PREPA under Title III.

As a result of the bankruptcy filing, the Partnership's non-recourse debt is in default and has been classified as current as of December 31, 2017.

Additionally, on July 18, 2017, Moody's downgraded the Partnership to Caa1 from B3 due to the heightened default risk for the Partnership as a result of PREPA's bankruptcy protection. This protection gives PREPA the ability to renegotiate contracts, which could impact the value of the assets in Puerto Rico or otherwise have a material impact on the Partnership.

The Partnership's receivable balances as of December 31, 2017 totaled $84.0 million, of which $50.9 million was overdue. Despite the disruption caused by the hurricanes and the Title III protection, PREPA has restarted the payments to the generators. The Partnership was able to collect $49.9 million of overdue amounts as of December 31, 2017.

In January 2018, Puerto Rico announced its intention to privatize PREPA. The plan will need to be approved by the Oversight Board, and, if approved, could take 18 months to complete. It is difficult to predict the outcome of the proposed privatization, but the impact at the Partnership could be material.

Considering the information available as of this financial statements, Management believes the carrying amount of the Partnership's assets of $604.8 million is recoverable as of December 31, 2017.

4. Related Party Transactions

Partnership occasionally enters into various transactions with affiliated companies. Related-party receivables of $331 and $319 and related-party payables of $9,784 and $8,537 are included in the accompanying balance sheets as of December 31, 2017 and 2016, respectively. In addition, the Partnership has a project management agreement with AES Solutions, LLC ("AES Solutions"), a related party, to obtain certain support services for the operations of the Plant. Management fees charged by AES Solutions to the Partnership during the years ended December 31, 2017 and 2016 amounted to approximately $3.5 million and $0.9 million, respectively. The Partnership did not pay dividends during 2017 and 2016.

5. Inventory, net

The following table summarizes inventory balances as of December 31, 2017 and 2016:

	2017	2016
Coal and raw materials	**$ 19,993**	$ 19,783
Spare parts and supplies	**7,108**	7,138
Total	**$ 27,101**	$ 26,921

6. Property, Plant and Equipment

The following represents a summary of property, plant and equipment as of December 31, 2017 and 2016:

	2017	2016
Land	**$ 5,074**	$ 5,074
Generation equipment	**792,280**	788,125
Buildings	**1,957**	1,975
Office, furniture and other equipment	**1,709**	1,306
Less: Accumulated depreciation	**(255,318)**	(237,911)
Construction in progress	**2,473**	4,299
Total property, plant and equipment, net	**$ 548,175**	**$ 562,868**

The movements of property, plant and equipment as of December 31, 2017 and 2016 is as follows:

	December 31, 2017					
	Land	Generation and equipment	Buildings	Office, furniture and other equipment	Construction in progress	Total
Cost:						
At the beginning of the year	$ 5,074	$ 788,125	$ 1,975	$ 1,306	$ 4,299	$ 800,779
Additions	—	—	—	—	5,469	5,469
Reclasses and adjustments	—	6,691	74	530	(7,295)	—
Sales and disposals	—	(2,536)	(92)	(127)	—	(2,755)
At the end of the year	5,074	792,280	1,957	1,709	2,473	803,493
Accumulated Depreciation:						
At the beginning of the year	—	236,807	341	763	—	237,911
Expense of the year	—	19,424	60	71	—	19,555
Sales and disposals	—	(2,128)	(9)	(11)	—	(2,148)
At the end of the year	—	254,103	392	823	—	255,318
Net Balance	**$ 5,074**	**$ 538,177**	**$ 1,565**	**$ 886**	**$ 2,473**	**$ 548,175**

(In Thousands of U.S. Dollars)

6. Property, Plant and Equipment (continued)

	December 31, 2016					
	Land	Generation and equipment	Buildings	Office, furniture and other equipment	Construction in progress	Total
Cost:						
At the beginning of the year	$ 5,074	$ 785,958	$ 1,826	$ 1,244	$ 2,702	$ 796,804
Additions	—	—	—	—	4,315	4,315
Reclasses and adjustments	—	2,507	149	62	(2,718)	—
Sales and disposals	—	(340)	—	—	—	(340)
At the end of the year	5,074	788,125	1,975	1,306	4,299	800,779
Accumulated Depreciation:						
At the beginning of the year	—	217,142	284	1,473	—	218,899
Expense of the year	—	19,232	57	63	—	19,352
Reclasses and adjustments	—	773	—	(773)	—	—
Sales and disposals	—	(340)	—	—	—	(340)
At the end of the year	—	236,807	341	763	—	237,911
Net Balance	$ 5,074	$ 551,318	$ 1,634	$ 543	$ 4,299	$ 562,868

Depreciation expense for the year ended December 31, 2017 and 2016 was $19,555 and $19,352, respectively. All of the PPE was pledged as a security for the Company's debt as of December 31, 2017 and 2016.

7. Other Intangible Assets

The following table summarizes the balances comprising intangible assets in the accompanying balance sheet as of the periods indicated:

	December 31,					
	2017			**2016**		
	Gross Balance	**Accumulated Amortization**	**Net Balance**	**Gross Balance**	**Accumulated Amortization**	**Net Balance**
Internal-use Software	1,987	(1,900)	87	1,981	(1,859)	122
Total	**$ 1,987**	**$ (1,900)**	**$ 87**	**$ 1,981**	**$ (1,859)**	**$ 122**

The movements of intangible assets is shown below:

	Internal use-software
Balance as of December 31, 2015	$ 223
Amortization	(101)
Balance as of December 31, 2016	$ 122
Additions	6
Amortization	(41)
Balance as of December 31, 2017	**$ 87**

(In Thousands of U.S. Dollars)

7. Other Intangible Assets (continue)

The following table summarizes the estimated amortization expense by intangible asset category for 2018 through 2022:

	2018	2019	2020	2021
Internal-use Software	41	40	36	1
Total	**$ 41**	**$ 40**	**$ 36**	**$ 1**

Intangible asset amortization expense was $41 and $101 for the years ended December 31, 2017 and 2016.

8. Long-Term Debt

As of December 31, 2017 and 2016, long-term debt consisted of the following:

	2017	2016
Bank loans	**$ 181,250**	$ 227,161
Revenue bonds	**193,400**	193,400
Total long-term debt	**374,650**	420,561
Deferred financing costs, net	**(3,126)**	(3,607)
Unamortized discount, net	**(6,050)**	(6,844)
Total long-term debt, net	**365,474**	410,110
Less current portion	**(18,611)**	(77,199)
Reclassification	**(346,863)**	—
Noncurrent portion	**$ —**	$ 332,911

As a result of the bankruptcy filing of PREPA described in Note 3 Concentration of Risk, the Partnership's non-recourse debt of $365,474 is in default and has been classified as current as of December 31, 2017.

Long-term debt, for which commitments were received and initial funding occurred in June 2000, consists of the Partnership's commercial bank loans (the "Bank Loans") that include loan commitments, working capital commitments and a letter of credit commitment provided by a syndicate of commercial banks with Calyon Corporate and Investment Bank as administrative agent, and revenue tax-exempt and taxable bonds (the "Bonds").

During April 2015, the Working Capital commitment of $25 million expired, as per contracted terms, became a quarterly amortizing loan with no penalties or default consequences. During 2012, the Partnership renewed the Total Reserve Commitment of $17.0 million through November 29, 2017. As of December 31, 2017 and 2016, the Reserve Commitment remain undrawn.

In Thousands of U.S. Dollars)

8. Long-Term Debt (continued)

Future maturities of long term debt at December 31, 2017, are as follows:

Year Ending December 31		Amount
2018	$	18,611
2019		31,568
2020		50,194
2021		39,127
2022		52,962
Thereafter		182,188
Total	$	374,650

Collateral for the long-term debt consists of all Plant and related facilities and all agreements relating to the operation of the project. The long-term debt agreements require the Partnership to comply with certain negative and affirmative covenants.

These covenants include restrictions over the Partnership's ability to pay distributions to the partners before debt service requirements are satisfied, among other restrictions. At December 31, 2017 and 2016, the Partnership was in compliance with the financial covenants.

Bank Loans

Bank loans accrue interest at the current floating rate for the selected rollover period. The Partnership pays interest expense ranging between 2.14% and 8.51% per annum on the outstanding balance of the bank loans. Prepayments are permitted.

The Bank loans are scheduled to be repaid as follows:

Bank Loan	Facility Amount	Outstanding Amount at December 31 2017	2016	Term
Tranche 2A and 2B construction loans	$ 491,094	$ 131,661	$ 167,957	Tranche 2A and Tranche 2B are due in quarterly installments. Tranche 2A matures November 29, 2017 and Tranche 2B matures November 29, 2020.
Tranche 2C construction loans	50,000	49,589	49,589	Due in quarterly installments of $6,199 commencing on May 25, 2021 through November 29, 2022.
Working capital loan	25,000	–	9,615	Due in quarterly installments of $1,923 commencing on April 2015 through November 2017.
Total		$ 181,250	$ 227,161	

8. Long-Term Debt (continued)

The Partnership had interest-rate swap agreements of which two expired on May 25, 2016 and five expired on June 30, 2017. In the event of nonperformance by the counterparties to the interest rate swap agreements, the Partnership may be exposed to increased interest rates. The Partnership continually evaluates the creditworthiness of its counterparties.

Bonds

The Bonds were issued through the Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority to finance a portion of the costs of developing, acquiring, constructing and equipping the Plant.

The tax-exempt bond ("2000 A Bond ") were used for financing the portions of the project consisting of solid waste disposal facilities, capitalized interest, reserve fund requirements, and issuance costs. The taxable bond ("2000 B Bond") were used for financing other portions of the project, capitalized interest, reserve fund requirements and issuance costs.

The tax-exempt bonds ("2000 A Bonds") accrue interest at the rate of 6.625% per annum and are due on June 1, 2026. The taxable bonds ("2000 B Bonds") accrue interest at the rate of 9.12% per annum and are due through June 1, 2022. The Bonds are subject to certain mandatory sinking fund requirements (see *Note 10*). The 2000 A Bonds are redeemable at the option of the Partnership, in whole or in part, at 100% of the redemption price, plus accrued interest to the redemption date.

The weighted average interest rate on the project financing debt for the years ended December 31, 2017 and 2016 was 5.92% and 6.46%, respectively.

9. Derivatives

Risk Management Objectives

The Partnership is exposed to market risks associated with its business activities, namely interest rate risk. In order to manage the market risks associated with these business activities, the Partnership enters into contracts that incorporate derivatives and financial instruments which consist of interest rate swaps.

The Partnership generally applies hedge accounting to all contracts as long as they are eligible under the accounting standards for derivatives and hedging. Derivative transactions are not entered into for trading purposes.

Interest Rate Risk

The Partnership utilizes variable rate debt financing for operations, resulting in an exposure to interest rate risk. Interest rate swap agreements are entered into to manage interest rate risk by effectively fixing or limiting the interest rate exposure on the underlying financing.

(In Thousands of U.S. Dollars)

9. Derivatives (continued)

These interest rate contracts expire in 2017, and are typically designated as cash flow hedges.

Accounting and Reporting

The following table sets forth the Partnership's derivative instruments as of December 31, 2017 and 2016 by type of derivative and by level within the fair value hierarchy. Derivative assets and liabilities are recognized at their fair value. All instruments are designated as hedging instruments.

	December 31, 2017				December 31, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**	Level 1	Level 2	Level 3	Total
Liabilities								
Current liabilities								
Interest rate derivatives	$ —	$ —	$ —	$ —	$ —	$ 857	$ —	$ 857
Total liabilities	$ —	$ —	$ —	$ —	$ —	$ 857	$ —	$ 857

The Partnership has elected not to offset net derivative positions in the financial statements.

The table below sets forth the pre-tax accumulated other comprehensive loss expected to be recognized as a decrease to income before income taxes over the next twelve months as of December 31, 2017 for interest rate derivatives:

	Accumulated Other Comprehensive Loss
Interest rate derivatives	$ (123)

The balance in accumulated other comprehensive loss ("AOCL") related to derivative transactions will be reclassified into earnings as interest expense is recognized for interest rate hedges. These balances are included in the statements of cash flows as operating activities based on the nature of the underlying transaction.

The following table sets forth the pre-tax losses recognized in AOCL and earnings related to the effective portion of derivative instruments in qualifying cash flow hedging relationships, including amortization of de-designated hedges, as defined in the accounting standards for derivatives and hedging, for the years ended December 31, 2017 and 2016:

(In Thousands of U.S. Dollars)

9. Derivatives (continued)

	Losses Recognized in AOCL				Location of Losses Reclassified from AOCL into Earnings	Losses Recognized from AOCL into Earnings			
		2017		2016			**2017**		2016
Interest rate derivatives	$	(2)	$	(256)	Interest expense	$	(1,451)	$	(8,393)
Total	$	(2)	$	(256)		$	(1,451)	$	(8,393)

The following table sets forth the pre-tax losses or gains recognized in earnings related to the ineffective portion of derivative instruments in qualifying cash flow hedging relationships, as defined in the accounting standards for derivatives and hedging, for the years ended December 31, 2017 and 2016:

	Classification in Statement of Income	Losses Recognized in Earnings			
			2017		2016
Interest rate derivatives	Interest expense	$	(5)	$	(129)
Total		$	(5)	$	(129)

The following table sets forth the pre-tax losses or gains recognized in earnings related to the not designated for hedge accounting portion of derivative instruments in qualifying cash flow hedging relationships, as defined in the accounting standards for derivatives and hedging, for the years ended December 31, 2017 and 2016:

	Classification in statement of comprehensive income	Losses Recognized in Earnings			
			2017		2016
Interest rate derivatives	Interest expense	$	(5)	$	(61)
Total		$	(5)	$	(61)

10. Contingencies and Commitments

Mandatory sinking fund

The Bonds are subject to semi-annual mandatory sinking fund redemption on each June 1 and December 1, beginning December 1, 2022 and June 1, 2021 for the 2000 A and 2000 B Bonds, respectively, at a redemption price equal to 100% of the principal amount of the Bonds called for redemption, without premium, together with accrued interest to the redemption date, as follows in the next page:

(In Thousands of U.S. Dollars)

10. Contingencies and Commitments (continued)

	Principal Amount to be Redeemed	
Redemption Date	2000 A Bonds	2000 B Bonds
June 1, 2021	$ —	$ 8,232
December 1, 2021	—	12,299
June 1, 2022	—	12,299
December 1, 2022	15,869	—
June 1, 2023	17,852	—
December 1, 2023	17,951	—
June 1, 2024	20,827	—
December 1, 2024	20,927	—
June 1, 2025	22,315	—
December 1, 2025	22,216	—
June 1, 2026	22,613	—
Total	$ 160,570	$ 32,830

Environmental

The Plant is subject to emission regulations, which may result in increased operating costs or the purchase of additional pollution control equipment if emission levels are exceeded. The Partnership periodically reviews its obligations for compliance with environmental laws, including site restoration and remediation.

Because of the uncertainties associated with environmental assessment and remediation activities, future costs of compliance or remediation could be higher or lower than the amount currently accrued.

Litigation

On March 9, 2009, the Governor of Puerto Rico signed Act No. 7, known as the "Special Act" to declare a state of fiscal emergency and to establish a comprehensive fiscal stabilization plan to salvage the credit of Puerto Rico. For fiscal years 2009-2011, a special tax on all real property was imposed by the Act. The special tax was imposed on 100% of the amount assessed and determined by the Municipal Revenue Collection Center. The Partnership paid to the Secretary of the Treasury the special tax related to the period 2009-2011 totaling $0.3 million.

On November 29, 2011, the Partnership requested and obtained a debt certificate from the Department of Treasury of Puerto Rico which stated that the Partnership had an outstanding liability of $4.9 million, which includes penalties and interest, relating to the special property tax, for which the Partnership disagrees and has not recorded as a liability. The Department of Treasury disagrees with the assessed value used by the Partnership.

10. Contingencies and Commitments (continued)

On March 8, 2016 the Partnership received a debt notice from the Department of Treasury of Puerto Rico where it reflected a debt of $6.6 million which include penalties and interest for years 2009-2011. The Partnership does not agree with the additional claim and presented its arguments against this claim to the Department of Treasury in March 2012. In addition, the Partnership is requesting that the $0.3 million payments made during 2009-2011 be refunded.

After various meetings with Department of Treasury's officials, the case is now pending that the corresponding clarifications and adjustments be made at the Municipal Revenues Collection Center (CRIM by its Spanish acronym). Once the adjustment is made, the debt should be eliminated from the Department of Treasury's record.

The Partnership is also involved in claims, suits and legal proceedings arising in the normal course of business. The Partnership has accrued for litigation and claims where it is probable that a liability has been incurred and the amount of loss can be reasonably estimated. The Partnership believes that the ultimate outcome of these proceedings and actions is unlikely to have a material adverse effect on the Partnership's financial statements.

11. Benefit Plan

The Partnership sponsors a defined contribution plan covering all employees who are at least 21 years old. Participants may contribute from one to ten percent of their annual compensation, as defined, up to the maximum amount allowed by local law. The Partnership matches participant contributions up to a maximum of five percent of the participant's compensation. The Partnership's contributions for the years ended December 31, 2017 and 2016 were not significant.

12. Share-Based Compensation

The Partnership participates in the stock-based compensation plans of AES that provides for grants of AES' stock options and restricted stock units to eligible participants. Awards under the Plan vest over periods ranging from two to five years. The compensation expense is recorded by applying the fair value recognition provisions. The expense related to stock-based employee compensation included in the determination of net income was $123 in 2017 and $93 in 2016.

13. Income Taxes

During December 2009, the Partnership's requested to have the grant amended to reduce the flat income tax rate from seven percent (7%) to four percent (4%). On July 20, 2010 4% tax rate was approved and the effective date of this amended was January 1, 2010.

(In Thousands of U.S. Dollars)

13. Income Taxes (continued)

Additionally the grant provides for 60% and 90% exemption from municipal license and property taxes, respectively, for a period of twenty (20) years commencing on July 1, 2004 and January 1, 2004 for municipal license and property taxes, respectively. Since for taxable years 2002 and 2003, no timely election was made to claim the benefits of the flexible tax exemption, then, the grant expires in the year 2022.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. These items are stated at the enacted tax rates that are expected to be in effect when taxes are actually paid or recovered.

The income tax provision consisted of the following for the years ended December 31, 2017 and 2016:

	2017	2016
Current income tax expense	$ 1,250	$ 2,645
Deferred income tax expense	(4)	(2,135)
Total income tax expense	**$ 1,246**	$ 510

The reconciliation between the Partnership effective tax rate on income from continuing operations and the statutory tax rate is as follows:

	2017	2016
Income tax expense at Decree rate	$ 1,078	$ 340
Exempt foreign source income	(37)	(38)
Non deductible expenses	5	2
Other current tax not exempt by Decree	200	205
Other permanent differences	—	1
Income tax expense	**$ 1,246**	$ 510

(In Thousands of U.S. Dollars)

13. Income Taxes (continued)

The following table summarizes the deferred tax assets and liabilities of the Partnership as of December 31, 2017 and 2016:

		2017		2016
Deferred Tax Assets:				
Allowance for Doubtful Accounts	$	19	$	1,067
Derivatives		—		34
Capitalized interest		203		209
Deferred revenue		4,227		3,571
Total deferred tax assets	$	4,449	$	4,881
Deferred Tax Liabilities:				
Depreciation of electric generation assets and others	$	20,473	$	20,846
Total deferred tax liabilities		20,473		20,846
Deferred tax liability - net	$	16,024	$	15,965

The Partnership believes that it is more likely than not that the deferred tax assets as shown above will be realized when future taxable income is generated through the reversal of existing taxable temporary differences and income that is expected to be generated by its long-term contract with PREPA. No valuation allowance has been established for deferred tax assets as of December 31, 2017 and 2016.

The Partnership's policy for interest and penalties related to income tax exposures is to recognize interest and penalties as a component of the provision for income taxes in the statement of comprehensive income. As of December 31, 2017, the Partnership believes that there are no uncertain tax positions and has no accrued income tax related interest and/or penalties in the accompanying 2017 balance sheet. The Partnership is potentially subject to income tax audits in the Commonwealth of Puerto Rico for taxable years from 2013 to 2017, until the applicable statute of limitations expire.

On December 25, 2013, the Governor of Puerto Rico signed Act. No 163 introducing significant requirements for supplementary schedules. The Act 163 also introduces new rules for the relationship of the certified public accounts and Puerto Rico Treasury Department and the deferral of the deduction for certain expenses paid to related parties. The Act is effective on December 25, 2013 and the supplementary information required should be include with the tax filing commencing after June 30, 2014.

14. Fair Value

The fair value of current financial assets and liabilities and debt service reserves approximate their reported carrying amounts. The fair value of long-term debt is estimated differently based upon the type of loan.

(In Thousands of U.S. Dollars)

14. Fair Value (continued)

In general, the carrying amount of variable rate debt is a close approximation of its fair value due to the short term nature of the interest rate. For fixed rate loans, the fair value is estimated using quoted market prices or discounted cash flow analysis.

The fair value of interest rate swaps is the estimated net amount that the Partnership would receive or pay to sell or transfer the agreements as of the balance sheet dates. The estimated fair values of the Partnership's liabilities have been determined using available market information. By virtue of these amounts being estimates and based on hypothetical transactions to sell assets or transfer liabilities, the use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The following table summarizes the carrying amount and fair value of certain of the Partnership's financial assets and liabilities as of December 31, 2017 and 2016:

	2017		2016	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value
Debt, net	**$ 365,474**	**$ 365,327**	$ 410,110	$ 412,056
Derivatives (1)	**—**	**—**	857	857
	$ 365,474	**$ 365,327**	$ 410,967	$ 412,913

(1) See the Partnership's fair value policy in Note 2 for further detail regarding fair value hierarchy.

Valuation Techniques

The fair value measurement accounting guidance describes three main approaches to measuring the fair value of assets and liabilities: (1) market approach; (2) income approach and (3) cost approach. The market approach uses prices and other relevant information generated from market transactions involving identical or comparable assets or liabilities. The income approach uses valuation techniques to convert future amounts to a single present value amount. The measurement is based on current market expectations of the return on those future amounts. The cost approach is based on the amount that would currently be required to replace an asset. The Partnership measures its derivatives at fair value on a recurring basis. Additionally, in connection with annual or event-driven impairment evaluations, certain nonfinancial assets and liabilities are measured at fair value on a nonrecurring basis. These include long-lived tangible assets (i.e., property, plant and equipment). In general, the Partnership determines the fair value of derivatives using the income approach. In the nonrecurring measurements of nonfinancial assets and liabilities, all three approaches are considered; however, the value estimated under the income approach is often the most representative of fair value.

14. Fair Value (continued)

Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Partnership's assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the determination of the fair value of the assets and liabilities and their placement within the fair value hierarchy levels.

Derivatives

When deemed appropriate, the Partnership manages its risk from interest rate fluctuations through the use of financial derivative instruments. The derivatives are interest rate swaps to hedge long-term debt to establish a fixed rate on variable rate debt. The Partnership is counterparty to over-the-counter derivatives, which only represent interest rate swaps. The income approach is used to estimate the cash flows over the remaining term of the contract. Those cash flows are then discounted using the relevant spot benchmark interest rate (such as LIBOR) plus a spread that reflects the credit or nonperformance risk.

This risk is estimated by the Partnership using credit spreads and risk premiums that are observable in the market, whenever possible, or estimated borrowing costs based on bank quotes, industry publications and/or information on financing closed on similar projects. To the extent that management can estimate the fair value of these assets or liabilities without the use of significant unobservable inputs, these derivatives are classified as Level 2.

The Partnership's methodology to fair value its derivatives is to start with any observable inputs; however, in certain instances, the published forward rates or prices may not extend through the remaining term of the contract, and management must make assumptions to extrapolate the curve, which requires the use of unobservable inputs, such as proxy commodity prices or historical settlements to forecast forward prices. In addition, in certain instances, there may not be third party data readily available which requires the use of unobservable inputs. Similarly, in certain instances, the spread that reflects the credit or nonperformance risk is unobservable.

The fair value hierarchy of an asset or a liability is based on the level of significance of the input assumptions. An input assumption is considered significant if it affects the fair value by at least 10%. Assets and liabilities are transferred to Level 3 when the use of unobservable inputs becomes significant. When the use of unobservable input is insignificant, assets and liabilities are classified as Level 2. Transfers between Level 3 and Level 2 are determined as of the end of the reporting period and result from changes in significance of unobservable inputs to calculate the Credit Valuation Adjustment ("CVA").

14. Fair Value (continued)

Nonfinancial Assets and Liabilities

For nonrecurring measurements derived using the income approach, fair value is determined using valuation models based on the principles of discounted cash flows ("DCF"). The income approach is most often used in the impairment evaluation of long-lived tangible assets. The Partnership has developed internal valuation models for such valuations; however, an independent valuation firm may be engaged in certain situations. In such situations, the independent valuation firm largely uses DCF valuation models as the primary measure of fair value though other valuation approaches are also considered.

A few examples of input assumptions to such valuations include macroeconomic factors such as growth rates, industry demand, inflation, exchange rates, and power and commodity prices. Whenever possible, the Partnership attempts to obtain market observable data to develop input assumptions. Where the use of market observable data is limited or not possible for certain input assumptions, the Partnership develops its own estimates using a variety of techniques such as regression analysis and extrapolations. For the years ended December 31, 2017 and 2016, the Partnership did not measure any nonfinancial assets under the income approach.

For nonrecurring measurements derived using the market approach, recent market transactions involving the sale of identical or similar assets are considered. The use of this approach is limited because it is often difficult to find sale transactions of identical or similar assets. This approach is used to corroborate the fair value determined under the income approach. For the years ended December 31, 2017 and 2016, the Partnership did not measure any nonfinancial assets under the market approach.

For nonrecurring measurements derived using the cost approach, fair value is typically determined using the replacement cost approach. Under this approach, the depreciated replacement cost of assets is determined by first determining the current replacement cost of assets and then applying the remaining useful life percentages to such cost. Further adjustments for economic and functional obsolescence are made to the depreciated replacement cost. This approach involves a considerable amount of judgment, which is why its use is limited to the measurement of a few long-lived tangible assets. Like the market approach, this approach is also used to corroborate the fair value determined under the income approach. For the years ended December 31, 2017 and 2016, the Partnership did not measure any nonfinancial assets under the cost approach.

Fair Value Considerations

In determining fair value, the Partnership considers the source of observable market data inputs, liquidity of the instrument, the credit risk of the counterparty and the risk of the Partnership's or its counterparty's nonperformance. The conditions and criteria used to assess these factors are:

14. Fair Value (continued)

Sources of market assumptions

The Partnership derives most of its market assumptions from market efficient data sources (e.g., Bloomberg). To determine fair value, where market data is not readily available, management uses comparable market sources and empirical evidence to develop its own estimates of market assumptions.

Market liquidity

The Partnership evaluates market liquidity based on whether the financial or physical instrument, or the underlying asset, is traded in an active or inactive market. An active market exists if the prices are fully transparent to market participants, can be measured by market bid and ask quotes, the market has a relatively large proportion of trading volume as compared to the Partnership's current trading volume and the market has a significant number of market participants that will allow the market to rapidly absorb the quantity of the assets traded without significantly affecting the market price.

Another factor the Partnership considers when determining whether a market is active or inactive is the presence of government or regulatory controls over pricing that could make it difficult to establish a market based price when entering into a transaction.

Nonperformance risk

Nonperformance risk refers to the risk that the obligation will not be fulfilled and affects the value at which a liability is transferred or an asset is sold. Nonperformance risk includes, but may not be limited to, the Partnership or counterparty's credit and settlement risk. Nonperformance risk adjustments are dependent on credit spreads, letters of credit, collateral, other arrangements available and the nature of master netting arrangements. The Partnership is counterparty to interest rate swaps which subject the Partnership to nonperformance risk.

The Partnership adjusts for nonperformance or credit risk on its derivative instruments by deducting a CVA. The CVA is based on the margin or debt spread of the Partnership or counterparty and the tenor of the respective derivative instrument. The CVA for asset positions is based on the counterparty's credit ratings and debt spreads or, in the absence of readily obtainable credit information, the respective country debt spreads are used as a proxy.

The CVA for liability positions is based on the Partnership's current debt spread, the margin on indicative financing arrangements, or in the absence of readily obtainable credit information, the respective country debt spreads are used as a proxy. All derivative instruments are analyzed individually and are subject to unique risk exposures.

(In Thousands of U.S. Dollars)

15. Risk and Uncertainties

In September 2017, Puerto Rico was severely impacted by Hurricanes Irma and Maria, disrupting the operations of the Partnership, and certain Distributed Energy assets.

As a result of the Hurricanes, PREPA has declared an event of Force Majeure. However, both units of the Partnership's plant are available to generate electricity which, in accordance with the PPAs, will allow AES Puerto Rico to invoice capacity, even under Force Majeure. Puerto Rico's infrastructure was severely damaged, including electric infrastructure and transmission lines. The extensive structural damage caused by hurricane winds and flooding is expected to take significant time to repair.

Due to the extensive damage from the hurricanes, energy demand in Puerto Rico has decreased and is expected to remain low until economic activity has recovered. Despite the decrease in demand, the Partnership has resumed generation and continues to be the lowest cost and EPA compliant energy provider in Puerto Rico. Therefore, the Partnership expects to continue to be a critical supplier to PREPA.

On October 24, 2017, the U.S. Congress approved a $37 billion emergency disaster relief bill which will allow the US Government to help victims from the hurricanes and assist with the infrastructure rebuild in the affected areas through the Federal Emergency Management Agency. This supplemental appropriation includes an allocation of $5 billion for the Disaster Assistance Direct Loan Program to assist local governments, like Puerto Rico, in providing essential services, such as reestablishing electricity.

In November 2017, the Partnership signed a Forbearance and Standstill Agreement with its lenders to prevent the lenders from taking any action against the company due to the default events. This agreement will expire on March 22, 2018.

16. Other Income and Expenses

The components of other income and expenses are summarized as follows:

	2017	2016
Allowance for other receivables	$ —	$ (26,223)
Other Income	—	32
Other Expenses	(97)	(187)
Total other expenses net	**$ (97)**	**$ (26,378)**

During the fourth quarter of 2016, the Partnership recognized a full allowance on a non-trade receivable as a result of payment delays and discussions with the counterparty. The allowance relates to certain reimbursements the Partnership was expecting in connection with a legal matter. Management believes the counterparty is obligated to pay and plans to continue to attempt to fully collect the non-trade receivable.

17. Subsequent Event

As of December 31, 2017 the Partnership's receivable balances totaled $84.0 million, of which $50.9 million was overdue. During 2018 the Partnership's received payments from PREPA for the total amount of $49.9 million.

Subsequent events have been evaluated through the date financial statements were available to be issued on April 30, 2018.