

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL
AREA DE ARCHIVO DIGITAL

MUNICIPIO DE ADJUNTAS
AUDITORIA 2005-2006
30 DE JUNIO DE 2006

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Case # 07-48771

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SINGLE AUDIT REPORTING PACKAGE
FOR THE YEAR ENDED JUNE 30, 2006**

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SINGLE AUDIT REPORTING PACKAGE
FOR THE YEAR ENDED JUNE 30, 2006**

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MUNICIPALITY OF ADJUNTAS
FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006

Carlos R. Diaz Negrón

Certified Public Accountant

MEMBER:

American Institute of Certified Public Accountants

Puerto Rico Society of Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

**To the Honorable Mayor and
Municipal Legislative Body
Municipality of Adjuntas
Adjuntas, Puerto Rico**

I have audited the financial statements of the governmental activities, each major funds, and the aggregate remaining fund information of the Municipality of Adjuntas as of and for the year ended June 30, 2006 which collectively comprise the basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. My responsibility is to express an opinion on these financial statements based on my audit. I did not audit the financial statements of the business-type activities. Those statements were audited by other auditors whose report has been furnished to me, and in my opinion, insofar as it relates to the amounts included for Valle Verde, is based solely on the report of the other auditors.

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

In my opinion, the financial statements referred to above present fairly, in all material respect the respective financial position of the governmental activities, each major funds, and the aggregate remaining fund information of the Municipality of Adjuntas as of June 30, 2006, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT (CONTINUED):

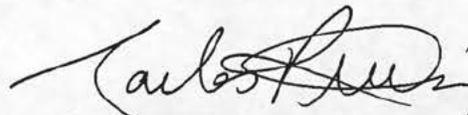
In accordance with Government Auditing Standards, I have also issued a report dated December 14, 2006, in my consideration of Municipality of Adjuntas's internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts grants agreements and other matters. The purposes of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of my audit.

The management's discussion and analysis and budgetary comparison information on pages 3 through 8 and 35 are not required part of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, I did not audit the information and express no opinion on it.

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Adjuntas's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the basic financial statements of the Municipality of Adjuntas. The schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

December 14, 2006
Aguas Buenas, Puerto Rico

License No. 1339
Expire December 1, 2007




CARLOS R. DIAZ NEGRON
CONTADOR PUBLICO AUTORIZADO
PUERTO RICO

The stamp No. 2204046 of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

**MUNICIPALITY OF ADJUNTAS, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006**

MANAGEMENT AND DISCUSSION ANALYSIS

Our discussion and analysis of the Municipality of Adjuntas (Municipality) financial performance provides an overview of the Municipality's financial activities for the year ended June 30, 2006. Please read it in conjunction with the financial statements, which begin on page 9.

FINANCIAL HIGHLIGHTS

- Beginning on January 2005, the Municipality of Adjuntas is under a new Administration. The elected and appointed officials have been performed a strict scrutiny of the economic and financial policies in effect to assure the maximum operational surplus and financial achievement.
- Also, the Statement of Net Assets for the Governmental Activities of the Municipality shows \$8.8 millions in capital assets. The capital assets of the Municipality are not pledged with neither long nor short-term liabilities.
- The Municipality has defendant of a lawsuit filed by approximately 82 individuals who claims political harassment and discrimination. During June 30, 2005 the Municipality paid \$1,365,000 under operational loans to 20 out of 82 plaintiffs. On November 2006 the jury determined in favor of the 62 plaintiffs for the amount of \$12,500,000. This sum must be paid within one hundred and twenty days from entry of this judgment.
- The Statement of Governmental Activities shows that the net assets of the Municipality decreased by \$12,479,088 for the period ended June 30, 2006 by the effect of litigation settlement. In the case of the Business-Type Activities, the net assets were reduced in \$1,824, basically for the effect of the depreciation expense, which totaled \$131,198.
- The most significant financial consideration related to the Financial Statements as a whole can be seen in the Statement of Revenues, Expenditures and Changes in Fund Balance of the General Governmental Fund. That report reflects that the Municipality ended its operations at June 30, 2006 with an excess of revenues over expenditures (surplus) of \$490,052. The operational surplus for the period ended June 30, 2006 for \$490,052 along with the accumulated surplus at the beginning of the year for \$1,159,314, totaled an accumulated surplus at the end of the year for \$1,649,366. See also the Balance Sheet for the General Fund, which shows an accumulated surplus totaling \$1,649,366 as of June 30, 2006.
- It is interesting to observe that in the Balance Sheet of Governmental Funds, the Municipality has in the State Legislative Joint Resolutions Fund, available cash totaling \$4.6 millions and total assets of \$5.4 millions to develop public works and perform special projects to benefit the Adjuntas' citizenship.

**MUNICIPALITY OF ADJUNTAS, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006**

GOVERNMENT-WIDE-FINANCIAL STATEMENT

The Government-Wide Financial Statements are designed to provide to readers with a broad overview of the Municipality's operations and finance as a whole in a manner similar to private-sector business. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at the end of the fiscal year. These financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means that these financial statements follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal year ended June 30, 2006 even if cash involved have not been received or paid. The Government-Wide Financial Statements include: (1) the Statements of Net Assets and (2) the Statement of Activities.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Assets and the Statement of Activities (on page 9 through 11) provide information about the activities of the Municipality as a whole and present a long-term view of the Municipality's finances. Fund financial statements start on page 12. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the Municipalities' operations in more detail than the government-wide statements by providing information about the Municipality's most significant funds.

Reporting the Municipality as a Whole

The Statement of Net Assets and the Statement of Activities

The Statement of Net Assets and the Statement of Activities report information about the Municipality as a whole and about its activities. These statements include *all* assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Municipality's *net assets* and changes in them. You can think of the Municipality's net assets, the difference between assets and liabilities, as one way to measure the Municipality's financial health or *financial position*. Over time, *increases or decreases* in the Municipality's net assets are one indicator of whether its *financial health* is improving or deteriorating. You will need to consider other non-financial factors, however, such as changes in the Municipality's property tax base and the condition of the roads, to assess the *overall health* of the Municipality of Adjuntas.

**MUNICIPALITY OF ADJUNTAS, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006**

In the Statement of Net Assets and the Statement of Activities, we grouped the Municipality's activities into:

- **Governmental Activities** – Most of the Municipality's basic services are reported here, including the municipal police, public works, garbage disposal, public energy and health services, and general administration. Property taxes, municipal license tax, state and federal grants finance most of these activities.
- **Business Activities** – The Municipality owns the Valle Verde Housing Project (Project), a housing development consisting of land, buildings and other improvements, which leases its 96 rental units to low and moderate income individuals in Adjuntas. The Project operates under Section 515 of USDA Rural Development (USDA-RD) Housing of the National Housing Act with HUD Section 8 Housing Assistance Payment Program.

Reporting the Municipality's Most Significant Funds

The Fund financial statements begin on page 12 and provide detailed information about the most significant funds, not the Municipality as a whole. Some funds are required to be established by bond covenants. The Municipality's basic services are reported in the governmental funds, that uses an accounting approach which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called *modified accrual accounting*, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed *short-term view* of the Municipality's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement on Activities) and governmental funds in Reconciliation of the Governmental Funds on page 16 of this report.

THE MUNICIPALITY AS A WHOLE

The Municipality's combined net assets decreased in the current year by \$ 12.6millions, to total \$2.2 million at end of year. Tables 1 and 2 focus on the net assets and changes in net assets of the Municipality's governmental and business-type activities for the current year.

**MUNICIPALITY OF ADJUNTAS, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006**

**Table 1
Net Assets
(In Millions)**

	<u>2005</u>	<u>2006</u>
Cash and other current assets	\$ 8.9	\$ 11.0
Other assets	.8	.8
Capital assets	<u>11.2</u>	<u>10.5</u>
Total assets	<u>20.9</u>	<u>22.3</u>
Short-term debt	2.5	4.2
Long-term debt	<u>7.7</u>	<u>20.4</u>
Total liabilities	<u>10.2</u>	<u>24.6</u>
Net Assets:		
Invested in capital assets, net of related debt	9.6	8.1
Restricted for:		
Debt service	.4	.4
State and Federal Programs	4.1	4.5
Revenue for replacement and others	.8	.8
Unrestricted	<u>(4.2)</u>	<u>(16.0)</u>
Total net assets	<u>\$ 10.7</u>	<u>\$(2.2)</u>

**Table 2
Changes in Net Assets
(In Millions)**

	<u>2005</u>	<u>2006</u>
Revenues		
Program revenues:		
Charge for services	\$.5	
Operating grants and contributions	2.0	1.8
Capital grants and contributions	4.6	2.3
General revenues:		
Property taxes	1.1	1.2
Municipal license tax	.3	.3
Grants and entitlements	4.6	4.5
Other income	<u>.6</u>	<u>.4</u>
Total Revenues	<u>13.7</u>	<u>10.5</u>
Program Expenses:		
General administration	3.8	3.6
Public safety	.3	.2
Education	1.9	1.5
Public works	5.0	3.9
Health and welfare	1.1	.9
Housing	.5	.5
Other	<u>.3</u>	<u>12.5</u>
Total Expenses:	<u>12.9</u>	<u>23.1</u>
Increase in Net Assets	<u>\$ 0.8</u>	<u>\$(12.6)</u>

**MUNICIPALITY OF ADJUNTAS, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006**

Net assets of the Municipality's governmental activities decreased by \$12.6 millions in the current year. *Unrestricted* net assets is the part of net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements.

Governmental Activities

The principal revenues of the Municipality are composed of property taxes and grant contributions. The Mayor of the Municipality of Adjuntas continued with an aggressive collections procedure especially in the property taxes area and submitted state and federal proposals to get competitive grant awards. Also, the Mayor of the Municipality implemented an adequate budget control and record keeping, which benefits the Municipality in its management decisions and operations. These are the main reasons to end operations with a significant surplus.

General Fund Budgetary Highlights

Once the Municipality's budget for the fiscal year 2005-2006 was approved on June 2005, the financial decisions were taken based on the available appropriations. However, during the course of the year, the Municipal Legislative Body revised the Municipality of Adjuntas' budget to adjust the original projections to the actual needs of the citizenship. The budget amendments fall into various categories. The first category includes transfers between expenditure accounts and the second one includes revisions to the amount of budget originally approved. The latest is related to additional revenues collected during the year, which exceeds the expectations originally included in the budget.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

As of June 30, 2006, the Municipality of Adjuntas had \$8.9 millions invested in a broad range of capital assets, including buildings, parks, roads, bridges and equipment. (See page 26)

**Table 3
Capital Assets at Year-End
(Net of depreciation, in Millions)**

	<u>Governmental Activities</u>	
	<u>2005</u>	<u>2006</u>
Land and land improvements	\$ 1.9	\$ 1.9
Buildings and improvements	5.9	5.7
Equipment	<u>1.6</u>	<u>1.3</u>
Totals	<u>\$ 9.4</u>	<u>\$ 8.9</u>

**MUNICIPALITY OF ADJUNTAS, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006**

More detailed information about the Municipality's capital assets is presented in Note 8 to the financial statements.

Long-Term Debt

At year-end, the Municipality had \$18.8 millions. in bonds, notes and other outstanding debts as shown in Table 4. (see page 27)

**Table 4
Outstanding Debt, at Year-end
(in Millions)**

	<u>Governmental Activities</u>	
	<u>2005</u>	<u>2006</u>
Bonds & Notes Payable	\$ 2.9	\$ 3.2
Other	<u>3.2</u>	<u>15.6</u>
Totals	<u>\$ 6.1</u>	<u>\$18.8</u>

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's elected and appointed officials considered many factors when setting the fiscal year 2006 budget. The most significant change in the next year's budget in comparison with the amounts included for the year ended June 30, 2006, is the increase in the estimated of municipal license and construction taxes. For these two revenue accounts the Municipality considered the taxes to be collected for the construction of various major projects as a part of the new administration governmental program.

We expect to end the operations for the fiscal year on June 30, 2007 with an additional surplus based on the economies in various budgeted expenditures accounts, which management has identified during the present year.

CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers and creditors with a general overview of the Municipality's finances and to show the accountability for the money it receives. If you have questions about this report or need additional financial information, contact us at the Municipality of Adjuntas, PO Box 1009, Adjuntas, Puerto Rico 00601.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
STATEMENT OF NET ASSETS
AS OF JUNE 30, 2006

PRIMARY GOVERNMENT

ASSETS	GOVERNMENTAL ACTIVITIES	BUSINESS -TYPE ACTIVITIES	TOTAL
Cash and cash equivalents	\$ 8,017,491	\$ 9,365	\$ 8,026,856
Cash with fiscal agent	975,827		975,827
Accounts receivable:			
Other government agencies	1,153,551		1,153,551
Property taxes	798,043		798,043
Other assets	9,212	2,549	11,761
Restricted cash		845,492	845,492
Capital assets, net	<u>8,847,487</u>	<u>1,680,947</u>	<u>10,528,434</u>
Total Assets	<u>19,801,611</u>	<u>2,538,353</u>	<u>22,339,964</u>
 LIABILITIES AND NET ASSETS			
Liabilities:			
Accounts payable and accrued expenses	1,401,958	40,421	1,442,379
Deferred revenue:			
Municipal patents	233,073		233,073
Federal funds	1,996,703		1,996,703
Due to other government agencies	528,819		528,819
Long-term debt:			
Due within one year	12,715,478	82,786	12,798,264
Due in more than one year	<u>6,104,065</u>	<u>1,464,516</u>	<u>7,568,581</u>
Total Liabilities	<u>22,980,096</u>	<u>1,587,723</u>	<u>24,567,819</u>
 Net Assets:			
Invested in capital assets, net of related debt	8,014,487	133,645	8,148,132
Restricted for:			
Debt service	368,509		368,509
Capital project	4,504,487		4,504,487
Revenue for replacement and others		845,492	845,492
Unrestricted	<u>(16,065,968)</u>	<u>(28,507)</u>	<u>(16,094,475)</u>
Total Net Assets	\$ (3,178,485)	\$ 950,630	\$ (2,227,855)

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2006**

<u>FUNCTIONS AND PROGRAMS</u>	<u>EXPENSES</u>	<u>PROGRAM REVENUES</u>			<u>NET (EXPENSE)/ REVENUE</u>
		<u>CHARGE FOR SERVICES</u>	<u>OPERATING GRANTS AND CONTRIBUTIONS</u>	<u>CAPITAL GRANTS AND CONTRIBUTIONS</u>	
Governmental activities:					
General administration	\$ 3,656,632		\$ 653,754		\$ (3,002,878)
Public safety	244,121		6,065		(238,056)
Education, culture and recreational	1,492,271	\$ 2,343	986,950		(502,978)
Public works and sanitation	3,932,780			\$2,334,138	(1,598,642)
Health and welfare	964,348		187,175		(777,173)
Litigation settlement	12,500,000				(12,500,000)
Interest	<u>255,660</u>				<u>(255,660)</u>
Total governmental activities	23,045,812	2,343	1,833,944	2,334,138	(18,875,387)
Business type-activities:					
Housing	<u>517,770</u>	<u>515,946</u>			<u>(1,824)</u>
Total	\$23,563,582	\$518,289	\$1,833,944	\$2,334,138	<u>\$(18,877,211)</u>

(Continue)

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
STATEMENT OF ACTIVITIES (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS-TYPE ACTIVITIES</u>	<u>TOTAL</u>
Net (expense)/revenue	<u>\$(18,875,387)</u>	<u>\$ (1,824)</u>	<u>\$(18,877,211)</u>
General revenue:			
Taxes:			
Property taxes	1,166,331		1,166,331
Municipal tax	279,783		279,783
Grants and entitlements	4,463,526		4,463,526
Other	<u>486,659</u>	<u> </u>	<u>486,659</u>
Total general revenues	<u>6,396,299</u>	<u> </u>	<u>6,396,299</u>
Changes in net assets	(12,479,088)	(1,824)	(12,480,912)
Net assets at beginning, as restated	<u>9,300,603</u>	<u>952,454</u>	<u>10,253,057</u>
Net assets at end	<u>\$ (3,178,485)</u>	<u>\$950,630</u>	<u>\$ (2,227,855)</u>

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
BALANCE SHEET
GOVERNMENTAL FUNDS
AS OF JUNE 30, 2006**

	GENERAL FUND	DEBT SERVICE FUND	STATE LEGISLATIVE JOINT RESOLUTIONS FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
Cash:					
Cash in bank	\$1,325,954		\$4,593,362	\$2,098,175	\$ 8,017,491
Cash with fiscal agent		\$356,827		619,000	975,827
Receivables:					
Amount due from:					
Interest			9,212		9,212
Governmental agencies				1,153,551	1,153,551
Other funds	1,143,716		824,310	642,008	2,610,034
Property tax	<u>585,492</u>	<u>158,160</u>	<u> </u>	<u> </u>	<u>743,652</u>
Total assets	\$3,055,162	\$514,987	\$5,426,884	\$4,512,734	\$13,509,767
Liabilities:					
Accounts payable and accrued expenses	\$ 369,446		\$ 766,527	\$ 220,806	\$ 1,356,779
Deferred revenues:					
Municipal patents	233,073				233,073
Property tax	542,249	\$146,478			688,727
Special funds				1,996,703	1,996,703
Due to other fund	158,939		774,870	1,676,225	2,610,034
Due to other government agency	<u>102,089</u>	<u> </u>	<u> </u>	<u> </u>	<u>102,089</u>
Total liabilities	<u>1,405,796</u>	<u>146,478</u>	<u>1,541,397</u>	<u>3,893,734</u>	<u>6,987,405</u>
Fund balance					
Reserve for:					
Debt service		368,509			368,509
Capital projects			3,885,487	619,000	4,504,487
Unreserved	<u>1,649,399</u>	<u> </u>	<u> </u>	<u> </u>	<u>1,649,366</u>
Total fund balance	<u>1,649,366</u>	<u>368,509</u>	<u>3,885,487</u>	<u>619,000</u>	<u>6,522,362</u>
Total liabilities and fund balance	\$3,055,162	\$514,987	\$5,426,884	\$4,512,734	\$13,509,767

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO THE STATEMENT OF NET ASSETS
AS OF JUNE 30, 2006**

Fund balances in governmental funds	\$ 6,522,362
<i>Amounts reported for governmental activities in the Statement of Net assets are different because:</i>	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	8,847,487
Deferred revenue in the governmental funds that are recorded as revenue in the statement of net assets.	688,727
Receivable recorded in the governmental activities are not available and therefore are not recorded in the funds financial statements.	54,391
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds:	
Bonds and notes payable	(3,273,180)
Compensated absences	(707,434)
Claims and judgments payable	(12,500,000)
Advances from CRIM	(1,683,827)
Due to PR Health Insurance Administration	(700,282)
Other accrued liabilities	<u>(426,729)</u>
<i>Net assets of governmental activities</i>	<u>\$ (3,178,485)</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE-GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2006**

	<u>GENERAL FUND</u>	<u>DEBT SERVICE FUND</u>	<u>STATE LEGISLATIVE JOINT RESOLUTIONS FUNDS</u>	<u>OTHER GOVERNMENTAL FUNDS</u>	<u>TOTAL GOVERNMENTAL FUNDS</u>
Revenues:					
Taxes:					
	\$ 863.588				
Property taxes		\$ 180.639			\$ 1,111,940
Municipal taxes	279.783				279,783
Grants and entitlements	4,463,524		\$1,120,000	\$2,889,846	8,473,370
Other	<u>475,391</u>	<u>11,268</u>	<u>160,581</u>		<u>647,240</u>
Total revenues	<u>6,149,999</u>	<u>191,907</u>	<u>1,280,581</u>	<u>2,889,846</u>	<u>10,512,333</u>
Expenditures:					
General administration	2,615,265			589,580	3,204,845
Public safety	243,482			639	244,121
Educational and recreational	408,372			1,083,899	1,492,271
Public works	1,340,222		1,552,175	1,091,372	3,983,769
Health sanitation and welfare	679,070		880	284,398	964,348
Debt service:					
Principal		292,000			292,000
Interest		150,414			150,414
Total expenditures	<u>5,286,411</u>	<u>442,414</u>	<u>1,553,055</u>	<u>3,049,888</u>	<u>10,331,768</u>
Excess of revenue over expenditures	<u>\$ 863,588</u>	<u>\$(250,507)</u>	<u>\$ (272,474)</u>	<u>\$ (160,042)</u>	<u>\$ 180,565</u>

(Continue)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE-GOVERNMENTAL FUNDS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

	<u>GENERAL FUND</u>	<u>DEBT SERVICE FUND</u>	<u>STATE LEGISLATIVE JOINT RESOLUTIONS FUND</u>	<u>OTHER GOVERNMENTAL FUNDS</u>	<u>TOTAL GOVERNMENTAL FUNDS</u>
Excess of revenues over expenditures	\$ 863,588	\$(250,507)	\$ (272,474)	\$(160,042)	\$ 180,565
Other financing sources (uses):					
Operating transfer in	9,947	223,441		160,042	393,430
Operating transfer out	(383,483)	(9,947)			(393,430)
Proceeds from loan				<u>619,000</u>	<u>619,000</u>
Total other financing sources	<u>(373,536)</u>	<u>213,494</u>		<u>779,042</u>	<u>619,000</u>
Excess of revenues and other financing source over expenditures and other financing sources	490,052	(37,013)	(272,474)	619,000	799,565
Fund balance at beginning of year	<u>1,159,314</u>	<u>405,522</u>	<u>4,157,961</u>		<u>5,722,797</u>
Fund balance at end of year	\$1,649,366	\$ 368,509	\$3,885,487	\$ 619,000	<u>\$6,522,362</u>

9/24/07
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The accompanying notes are an integral part of these financial statements.

316,777

476,411.00
159,

159,674-

221,043

206,796

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL
FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2006**

Net change in fund balances – total governmental funds	\$ 799,565
<i>Amounts reported for Governmental Activities in the Statement of Activities are different because:</i>	
Governmental funds report capital outlays as expenditures. However, in the statement of activities and changes in net assets, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount of capital assets recorded in the current period.	50,990
Governmental funds report principal payments on long-term debts as expenditures, where as the principal payments reduce the long-term debt in the statement of net assets.	292,000
Governmental funds report payment of other long-term debt as expenditure where as term debt in the statement of net assets.	25,819
Amount receivable from other agencies that are not available in the funds financial statements.	54,391
Change in accrued expense which does not require the use of current financial resources:	
Compensating absences	59,736
Litigation settlement	(12,500,000)
Governmental funds report payments of other long-term debt as expenditures where as the payment reduces the long-term is the obligate in the statement of net assets.	(13,688)
Proceed from issuance of a note was recorded as other financial sources in the funds financial statements, but the note increase long-term liabilities in the statement of net assets.	(619,000)
Depreciation expense on capital assets is reported in the statement of activities, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in governmental funds.	<u>(628,899)</u>
<i>Changes in Net Assets of Governmental Activities</i>	<u>\$(12,479,088)</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2006

1. ORGANIZATION

The Municipality of Adjuntas (the Municipality) is a political and legal entity with full legislative and administrative faculties in every affair of municipal character, with personal succession, existence and legal personality separate and independent from the governmental of the Commonwealth of Puerto Rico.

The municipal government is comprised of the executive and legislative bodies, which are elected every four years in the Puerto Rico general elections. The executive power is exercised by the Mayor and the legislative power by the Municipal Legislative Body, which has twelve members.

The Municipality provides the following services to its community: health, public works, education, public safety, housing, community and social services, welfare, culture and recreation, as well as many other general and administrative services.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Municipality relating to the funds included in the accompanying basic financial statements conform to accounting principles generally accepted in the United States of America applicable to state and local governments. Generally accepted accounting principles for local governments include those principles prescribed by the Governmental Accounting Standards Board (GASB), the American Institute of Certified Public Accountants in the publication entitled Audits of State and Local Governmental Units and by the Financial Accounting Standards Board (when applicable). The more significant policies of the Municipality are described below.

Reporting entity

A reporting entity consists of the primary government, component units, and other organization that are included to ensure that financial statements are not misleading. The primary government of the Municipality consists of all funds and departments that are not legally separate from the Municipality. For the Municipality of Adjuntas, these include various services such as police protection, recreation (including parks), street maintenance and repair, sanitation, and general administrative services. The operation of each of these activities is directly controlled by the Municipality's Legislative Body through the budgetary process.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Component units are legally separate organizations for which the Municipality is financially accountable. The Municipality has no component units.

Government wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all the activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities which normally are supported mainly by taxes and intergovernmental revenues are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include a) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

The fund financial statement segregates transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

The Municipality reports the following major governmental funds:

1) General Fund

This is the operating fund of the Municipality and accounts for all financial resources, except those required to be accounted for in another fund.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2) Debt Service Fund

This fund accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

3) State Legislative Joint Resolutions Fund

This fund accounts for revenue sources provided by the Commonwealth of Puerto Rico Legislature for the development of capital projects and other community services.

Measurement focus, basis of accounting and financial statement presentation

The government-wide financial statement of Net Assets and the Statement of Activities, both government and business like activities, are presented using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time the liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The governmental fund financial statements are presented using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Under this method revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, except for debt service, compensated absences and claims and judgments expenditures which are reported when payment is due.

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Measurement focus, basis of accounting and financial statement presentation (continued)

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The government has elected not to follow subsequent private sector guidance.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

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

Cash, cash equivalents, cash with fiscal agent and investment

The Municipality's finance director is responsible for investing available resources. The Municipality is restricted by law to invest only in savings accounts and certificates of deposit with banks qualified as a depository of public funds by the Puerto Rico Treasury Department (PRTD) or in instruments of the Government Development Bank for Puerto Rico (GDB). The Municipality's policy is to invest any excess cash in interest bearing deposits with institutions qualified by the PRTD. Earnings from these funds are recorded in the corresponding fund as interest income.

Cash with fiscal agent in the governmental fund consists of unused proceeds from bonds and notes issued for the acquisition and construction of major capital improvements. Cash with fiscal agent in the debt service fund represents special additional property tax collections retained by the Municipal Revenue Collection Center (CRIM) and restricted for the payment of the Municipality's debt service, as established by law.

The Municipality considers all investments with an original maturity of three months or less to be cash equivalents..

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Interfund receivables and payables

Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either due to/from other funds (i.e., the current portion of interfund loans) or advances to/from other funds (i.e., the non-current portion of interfund loans). Interfunds receivables and payables between funds within the governmental activities are eliminated in the statement of net assets.

Capital assets

Capital assets, which include property, plant, equipment, and infrastructure (which is normally immovable and of value only to the Municipality, such as roads, bridges, streets sidewalks, and drainage system), are reported in the applicable governmental columns in the government-wide financial statements. The Municipality has elected to not capitalize infrastructure acquired before the implementation date of GASB 34 (July 1, 2003).

Capital assets purchased or acquired are carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date donated. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. When historical cost is not available it is estimated using historic sales of the year of the acquisition of the related capital assets.

Depreciation in capital assets is calculated on the straight-line basis over the following estimated useful lives:

Building	50-40 years
Equipment and vehicles	5-10 years
Infrastructure	40 years

The Municipality decides when to capitalize an asset using a capitalization threshold of \$25.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reservation of fund balance

Reservations of fund balance represent portions of fund balances that are legally segregated for a specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:

1) Debt/ service

Represents net assets available to finance future debt service payments.

2) Capital projects

Represents the reservations of amounts available under state grant programs and loans for capital projects.

Risk financing

The Municipality carries insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center (the "CRIM") for the year ended June 30, 2004 amounted to approximately \$93,773. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$240,385 for workers compensation insurance covering all municipal employees.

Compensated absences

Employees accumulate vacation leave at a rate of 2.5 days per month up to maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum 90 days. In the event of employee resignation, the employee is paid for accumulated vacations days up to the maximum allowed.

Separation from employment prior to use of all or part of the sick leave terminates all rights for compensation, except for employees with ten years or more of service who are entitled to sick leave pay up to the maximum allowed.

Employees' maximum allowed vacations and vested sick benefits are accounted for in the Statement of Net Assets.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of estimates

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

3. PROPERTY TAX

The personal property tax is self assessed by the taxpayer on a return, which is to be filed by May 15 of each year with the Municipal Revenue Collector Center (the CRIM), a governmental entity created by the Commonwealth of Puerto Rico. Real property tax is assessed by the CRIM on each piece of real state and on each building.

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1.

The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Before the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, where by a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers.

This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM REMITS TO THE municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a liability to the CRIM is recorded at June, 30.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempt amounts, the Puerto Rico Treasury Department assumes payment of the basic tax to the Municipalities, except for property assessed at less than \$3,500 for which no payment is made. As part of Law No. 83 of August 30, 1991, as amended, the exempt amount to be paid by Puerto Rico Treasury Department to the Municipalities was frozen as of January 1, 1992. In addition, the law grants a tax exemption from the payment of personal property taxes of up to \$50,000 of the assessed value to retailers having annual net sales of less than \$150,000.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

3. PROPERTY TAX (CONTINUED)

The annual rate for fiscal year 2006 is 8.53% for real property and 6.53% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 6.0% and 4.0%, respectively, represent the Municipality's basic property tax rate, which is appropriated for general purposes and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico Electronic Lottery and subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities: (b) 1.50% represents the special ad valorem tax restricted for debt service and accounted for in the debt service fund. The Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected.

On January 26, 2000, Public Law 42, as amended, was enacted which authorized the CRIM to obtain a loan up to \$200 million, and for a term not exceeding 30 years, to allow for the financing of the debt that the municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances vs. actual collections through fiscal year 2000-2001. The amount that the municipalities will collect from the additional property taxes resulting from the increase in the subsidy from the central government to the municipalities was assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law 238, enacted on August 15, 1999. As of June 30, 2006, the amount due to CRIM amounting to \$1,683.827 is presented as other long-term debt (see Note 9).

4. VOLUME OF BUSINESS TAX

The municipal license tax is levied annually based on the volume of business of certain businesses and industrial organizations that operate in the Municipality. The tax rates are 1.50% for financing institutions and .50% for the other business institutions. The taxpayers must file a return not later than April 15 of every year and the tax is payable in two installments, due in July 1 and January 1 of the following fiscal year. The amount levied could be paid with a five percent (5%) discount if payment is made on or before the filing date. The Municipality levied and collected during the year ended June 30, 2006, \$233,073 corresponding to the following fiscal year volume of business tax. This amount was recorded as deferred revenue.

5. INTERGOVERNMENTAL REVENUES

Intergovernmental revenues sources consist of contributions received from certain quasi-public corporations of the Commonwealth of Puerto Rico, such as the Puerto Rico Aqueduct and Sewer Authority and the Puerto Rico Electric Power Authority. Also, the Municipality receives some subsidies from the Commonwealth of Puerto Rico which include, among others, a subsidy for general operations and for the financing of capital improvements. The intergovernmental revenues are recorded in the General fund, except for those that are legally restricted for expenditure for specified purposes which are recorded in the Other Governmental Funds.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

6. DEFERRED REVENUE

Municipal Tax

The deferred revenue of \$233.073 in the general fund is related to the municipal license tax collected in the fiscal year 2005-2006 corresponding to the following fiscal year.

Special Funds

The deferred revenue presented in other governmental funds is the portion grants received for which qualifying expenditures have not been incurred.

Property Tax

The deferred revenue of \$688.727 for property tax in the governmental funds represents property tax receivable and not available.

7. RESTRICTED DEPOSIT

Restricted cash in the business-type activities consists of:

Escrow deposit	\$ 22,093
Tenant security deposits	14,748
Reserve for replacement	802,605
Residual receipts	<u>6,046</u>
	<u>\$845,492</u>

Under the term of the Administrative Order, the Project is required to set aside specified amounts and the surplus cash deposits for the replacement of property and other project expenditures as approved by USDA-Rural Development.

The Project maintains a restricted cash account for insurance escrow. In addition, all tenant security deposits are deposited into a separate bank account and held in trust for the tenants until they vacate the property. Any amounts not returned to the tenant due to leave violations are transferred to the Projects' general operating account. Restricted funds are held in separate accounts and are not available for operating purposes. Substantially all restricted funds are invested in saving accounts, certificates of deposits and money market funds.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

8. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2006 was as follows:

Primary Government	Balance June 30, 2005	Increases	Decreases	Balance June 30, 2006
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 1,893,680			\$ 1,893,680
Capital assets being depreciated:				
Buildings	7,286,721			7,286,721
Equipment and vehicles	3,131,296	\$ 50,989		3,182,285
Total capital assets being depreciated	10,418,017	50,989		10,469,006
Less accumulated depreciation for:				
Buildings	1,417,167	154,543		1,571,710
Equipment and vehicles	1,469,133	474,356		1,943,489
Total	2,886,300	628,899		3,515,199
Total depreciable capital assets, net	7,531,717	(577,910)		6,953,807
Governmental activities capital assets net	9,425,397	(577,910)		8,847,487
Business-type activities:				
Capital assets net being depreciated:				
Land	362,859			362,859
Capital assets being depreciated:				
Building and improvements	3,983,215			3,983,215
Equipment	470,307	4,578		474,885
	4,453,522	4,578		4,458,100
Less accumulated depreciation:				
Building and improvements and equipment	3,008,814	131,198		3,140,012
Total depreciation, capital, assets net	1,444,708	(126,620)		1,318,088
Business activities capital assets, net	\$ 1,807,567	\$(126,620)	\$	\$ 1,680,947

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

8. CAPITAL ASSETS (CONTINUED)

Depreciation expense was charged to functions/programs of the Municipality as follows:

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>
General administration	\$ 54,940	
Public safety	70,942	
Public works	244,738	
Education, culture and recreation	229,358	
Health, sanitation and welfare	28,921	
Housing	_____	<u>\$131,198</u>
Total depreciation expense	<u>\$628,899</u>	<u>\$131,198</u>

9. LONG-TERM DEBTS

Long-term liability activity for the year ended June 30, 2006 was as follows:

Primary Government Governmental activities:	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due within one year</u>
Notes and bonds payable	\$2,901,000	\$ 619,000	\$292,000	\$ 3,228,000	\$ 189,000
Other long-term debt:					
Claims and judgments payable		12,500,000		12,500,000	12,500,000
Compensated absences	767,170		59,736	707,434	
Amount due to:					
CRIM	1,709,646		25,819	1,683,827	26,478
PR Health Insurance Administration	<u>700,282</u>	_____	_____	<u>700,282</u>	_____
Total	6,078,098	13,119,000	377,555	18,819,543	12,715,478
Business-type activities:					
Mortgage payable	<u>1,626,452</u>	_____	<u>79,150</u>	<u>1,547,302</u>	<u>82,786</u>
Total	\$7,704,550	\$13,119,000	\$456,705	\$20,366,845	\$12,798,264

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

9. LONG-TERM DEBTS (CONTINUED)

Governmental activities:

A. Notes and Bonds:

\$245,000 public improvement serial bond of 1988 payable in annual installments of \$14,000 to \$17,000 through January 2011 plus interest at 5%.	\$ 77,000
\$595,000 public improvement serial bonds of 1988 payable in annual installments ranging from \$34,000 to \$42,000 through January 1, 2011, plus interest at 5%.	187,000
\$200,000 public improvement serial bond of 1991 payable in annual installments ranging from \$9,000 to \$15,000 through January 1, 2015, plus interest at 5%.	104,000
\$465,000 public improvement serial bond of 1995 payable in annual installments ranging from \$40,000 to \$55,000 through July 1, 2009, plus interest at 6.20%	185,000
\$1,355,000 Special Fund for Loans to Governmental Entities payable in quarterly installments ranging from \$19,000 to \$20,000 through April 1, 2013, plus interest at 8%.	533,000
\$400,000 Special Fund for Loans to Governmental Entities payable in annual installments ranging from \$20,000 to \$40,000 through January 1, 2015, plus interest at 4.5%	265,000
\$1,365,000 Special Fund for Loans to Governmental Entities payable in annual installments ranging from \$35,000 to \$85,000 through July 1, 2029 plus interest at 5%.	1,330,000
\$619,000 Special Obligation Note payable in annual installments ranging from \$77,000 to \$106,000 through July 1, 2012, plus interest at Libor 90 days plus 1.25%.	<u>547,000</u>
	<u>\$3,228,000</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

9. LONG-TERM DEBTS (CONTINUED)

The annual debt service requirements to maturity bonds and notes payables of June 30, 2006 are as follows:

Notes and Bonds Payable <u>Year ended June 30</u>	Governmental –type Activities	
	<u>Principal</u>	<u>Interest</u>
2007	\$ 189,000	\$ 147,354
2008	313,000	155,713
2009	324,000	132,962
2010	349,000	116,055
2011	309,000	99,525
2012-2016	784,000	318,825
2017-2021	310,000	198,500
2022-2026	330,000	120,200
2027-2030	<u>320,000</u>	<u>29,925</u>
	<u>\$3,228,000</u>	<u>\$1,319,059</u>

Advances from CRIM

This amount represents the balance owed to CRIM at June 30, 2006 as described in Note 3 and is payable in monthly installments of \$10,922 through 2032 including interest at 6.1%. The advances from CRIM matures as follows:

<u>Year ended June 30</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 26,478	\$ 103,771
2008	28,989	102,056
2009	30,832	100,233
2010	32,769	98,296
2011	34,828	93,437
2012-2016	209,848	445,478
2017-2021	285,002	370,729
2022-2026	386,070	269,356
2027-2031	523,339	131,860
2032-2033	<u>125,672</u>	<u>5,841</u>
	<u>\$1,683,827</u>	<u>\$1,721,057</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006**

9. LONG-TERM DEBTS (CONTINUED)

Health Reform Insurance Liability

The amount due to the Puerto Rico Health Insurance Administration is related with a unpaid balance from year ended at June 30. 1997 arose from with the implementation of Act No. 72 of September 7, 1993, which established contributions for the medical services covered by the Health Reform based on the operational budget of the municipalities. The unpaid balance will be amortized through the proportional participation of the municipalities to the annual increase in electronic lottery income which will be collected and withheld by the Treasury Department of Puerto Rico.

Business-type activities:

Mortgage note payable in monthly installments of \$17,157 including interest at 8% through 2018. The note is collateralized by land and building.

\$1,547,302

Mortgage note payable matures as follows:

<u>Year ended June 30</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 82,786	\$110,916
2008	89,794	114,255
2009	97,394	106,650
2010	105,638	98,414
2011	114,580	89,494
2012-2016	743,925	285,495
2017-2018	<u>313,185</u>	<u>21,565</u>
	\$1,547,302	<u>\$826,789</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

10. RETIREMENT SYSTEM

Defined Benefit Pension Plan

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

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation. Disability benefits are available to members for occupational and non-occupational disabilities. However, a member must have at least ten years of service to receive non-occupational disability benefits.

Members who have attained at least 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have completed ten years of creditable services are entitled to an annual benefit, payable monthly for life. The amount of the annuity shall be one and one-half percent of the average compensation, as defined, multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined, otherwise they will receive 75 percent of the average compensation, as defined.

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

10. RETIREMENT SYSTEM (CONTINUED)

Defined Contribution Plan

The Legislature of the Commonwealth enacted Act No. 305 on September 24, 1999, which amends Act No. 447 to establish, among others, a defined contribution savings plan program (the "Program") to be administered by the Retirement System. All regular employees hired for the first time on or after January 1, 2000 and former employees who participated in the defined benefit pension plan and are rehired on or after January 1, 2000 become members of a Program as a condition to their employment received a refund of their contributions. In addition, employees who at December 31, 1999 were participants of the defined pension plan, had the option, up to March 31, 2000, to irrevocably transfer their prior contributions to the defined benefit pension plan plus interest thereon to the Program.

Act No. 305 requires employees to contribute 8.275% of their monthly gross salary to the Program. Employees may elect to increase their contribution up to 10% of their monthly gross salary. Employee contributions are credited to his/her individual account established under the Program. Participants have three options to invest their contributions to the Program. Investment income is credited to the participant's account semi-annually.

The Municipality is required by Act No. 305 to contribute 9.275% of the participant's gross salary. The Retirement System will use these contributions to increase its asset level and reduce the unfunded status of the defined benefit pension plan.

Upon retirement, the balance in the participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life and 50% of such benefits to the participant's spouse in case of the participant's death. Participants with a balance of \$10,000 or less at retirement will receive a lump-sum payment. In case of death, the balance in the participant's account will be paid in a lump-sum to his/her beneficiaries. Participants have the option of a lump-sum or purchasing an annuity contract in case of permanent disability.

Total employee and employer contributions to the above mentioned plans during the year ended June 30, 2006 amounted to approximately \$180,088 and \$214,348, respectively. This amount represented 100% of the required contribution for the corresponding year.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2006, a copy of which can be obtained from the Retirement System.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
JUNE 30, 2006

11. CONTINGENCIES AND SUBSEQUENT EVENT

Amounts received or receivable from grantor agencies are subject to audit and adjustment by grantor agencies. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of the expenditures which may be disallowed by the grantor cannot be determined at this time, although the Municipality expects such amounts, if any, to be immaterial.

The Municipality is defendant and /or codefendant in several litigations arising out of the normal Municipality's operations. Most of the cases are covered by insurance. Management, after consultation with legal counsel is of the opinion that the ultimate liability, in excess of insurance coverage, if any, resulting from such pending litigations will not have a material adverse effect on the Municipality's financial position.

The Municipality has been named defendant of a lawsuit filed by approximately 82 individuals who claim political harassment and discrimination. On December 3, 2001 the jury determined in favor of 20 out of 82 plaintiffs for the amount of \$6,956,400 for the remaining 62 plaintiffs. During the year the ended June 30, 2005, the Municipality paid the amount of \$1,500,000 to the plaintiffs. This amount was paid under an operating loan of \$1,365,000 and the remaining amount was paid with general funds. In addition, the Puerto Rico Secretary of Justice Ordered to the Puerto Rico Treasury Department to paid the remaining amount. The parties have informed the Court they have settled the claims, and that the Municipal Legislature has approved the settlement. On November 2006 the jury determined in favor of the 62 plaintiffs for the amount of \$12,500,000. This sum must be paid within one hundred and twenty days from entry of this judgment. Accordingly, a liability of \$12,500,000 has been recorded in the governmental activities financial statement.

12. RESTATEMENT OF FUND BALANCE

The fund balance of governmental activities as presented in 2005 statement of net assets has been adjusted because deferred revenue and receivable from property taxes were understated by \$222,754 and \$688,727, respectively and amount due from other agencies was overstated by \$954,301. The correction has no effect on the results of the current year's activities, however, the cumulative effect decrease beginning fund balance by \$488,328. In addition, the error on amount due to the other agency has been adjusted in governmental fund financial statements.

REQUIRED SUPPLEMENTARY INFORMATION

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SCHEDULE OF BUDGETARY COMPARISON
FOR THE YEAR ENDED JUNE 30, 2006**

	<u>GENERAL FUND</u>			
	<u>ORIGINAL BUDGET</u>	<u>BUDGET</u>	<u>ACTUAL</u>	<u>VARIANCE WITH FINAL BUDGET FAVORABLE (UNFAVORABLE)</u>
Revenues:				
Taxes:				
Property taxes	\$ 888,058	\$ 888,058	\$ 931,301	\$ 43,243
Municipal tax	281,064	281,064	279,783	(1,280)
Grants and entitlements	5,203,676	5,203,676	4,473,471	(730,205)
Other	<u>317,850</u>	<u>317,850</u>	<u>475,391</u>	<u>157,541</u>
Total revenues	<u>6,690,648</u>	<u>6,690,648</u>	<u>6,159,946</u>	<u>(530,702)</u>
Expenditures:				
General administration	3,867,836	3,920,166	2,615,265	1,304,901
Public safety	295,920	295,920	243,482	52,438
Education, culture and Recreational	437,210	437,210	408,372	28,838
Public works and sanitation	1,298,693	1,298,693	1,340,222	(41,527)
Health and welfare	521,714	521,714	679,070	(157,356)
Debt service	139,275	139,275	223,441	(84,166)
Transfer out	<u>130,000</u>	<u>77,668</u>	<u>160,042</u>	<u>(82,374)</u>
Total expenditures	<u>6,690,648</u>	<u>6,690,648</u>	<u>5,669,894</u>	<u>1,020,754</u>
Excess of revenue over expenditure	\$ _____	\$ _____	\$ 490,052	\$ 490,052

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO SCHEDULE OF BUDGETARY COMPARISSON
JUNE 30, 2006

1. BUDGETS AND BUDGETARY ACCOUNTING

The Municipality follows these procedures in establishing the budgetary data reflected in the financial statements:

- 1) Formal budgetary integration is employed as a management control device during the year for the General Fund. Formal budgetary integration is not employed for special revenue funds because effective budgetary control is alternatively achieved through legal and contractual grant requirements provisions.
- 2) On or before May 15, the Mayor submits to the Municipal Legislative Body a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means for financing them.
- 3) Public hearing are conducted at the Municipal Legislative Body to obtain citizens comments.
- 4) Prior to June 13, the budget is legally enacted through passage of an ordinance.
- 5) The Municipal Legislative Body approves, by ordinance budget appropriations by functional basis. The Mayor is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that alter the total appropriations of any fund must be approved by the Municipal Legislative Body.
- 6) Unused appropriations for the annual budgeted funds lapse at the end of the year.

The budget is prepared on the budgetary basis of accounting. The actual results of operations, presented in the Statement of Revenues and Expenditures – Budget and Actual General Fund, is in conformity with the budgetary accounting of the Municipality for a better comparison with the budget information.

The presentation of the budgetary data excludes other appropriations such as capital projects, debt service and special revenue funds because projects are funded on a multi-year nature, generally requiring several years to complete or effective budgetary control is alternatively achieved through general obligation bond indentures and legal and contractual grant agreement provisions.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO SCHEDULE OF BUDGETARY COMPARISSON (CONTINUED)
JUNE 30, 2006**

2. RECONCILIATION OF GAAP TO BUDGETARY BASIS

Adjustments necessary to reconcile the revenues and expenditures of the General Fund at the end of the year, from the generally accepted accounting principles to budgetary basis, are as follows:

	<u>Revenues</u>	<u>Expenditures</u>
Generally accepted accounting principles (GAAP) basis	\$6,149,999	\$5,286,411
Transfer in concluded as revenues expense in budgetary basis	<u>9,947</u>	<u>383,483</u>
Budgetary basis	<u>\$6,159,946</u>	<u>\$5,669,894</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2006

**MUNICIPALITY OF ADJUNTAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2006**

	<u>NUMBER</u>	<u>DISBURSEMENT</u>
<u>US Department of Housing and Urban Development</u>		
Passed through:		
Municipal Service Administration:		
Community Development Block Grant/ State Grant	14.228	\$ 671,713
Direct Program:		
Section 8 – Housing Choice Vouchers	14.871	187,175
 <u>US Department of Health and Human Services</u>		
Passes through:		
PR Department of Family:		
Child Care and Development Block Grant	93.575	50,366
Direct Program:		
Head Start	93.600	1,008,077
 <u>US Department of Agruculture</u>		
Passes through:		
Puerto Rico Department of Education		
Child an Adult Care Food Program	10.558	84,824
 <u>US Department of Home and Security</u>		
Passes through:		
PR Office of Management and Budget (GAR)		
Public Assistance Grant	97.036	<u>9,018</u>
		 <u>\$2,011,173</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2006

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Adjuntas and is presented on the cash basis of accounting. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, Audit of States, Local Governments and Non profit organizations. Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of the financial statements.

**REPORT ON INTERNAL
CONTROL OVER FINANCIAL REPORTING
BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

Carlos R. Diaz Negrón

Certified Public Accountant

MEMBER:

**American Institute of Certified Public Accountants
Puerto Rico Society of Certified Public Accountants**

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**REPORT ON INTERNAL
CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL
STATEMENT PERFORMED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARD**

**To the Honorable Mayor and
Municipal Legislative Body
Municipality of Adjuntas
Adjuntas, Puerto Rico**

I have audited the financial statements of governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the **Municipality of Adjuntas, Puerto Rico**, as of and for the year ended June 30, 2006 which collectively comprise the Municipality of Adjuntas's basic financial statements and have issued my report there on dated December 14, 2006. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing my audit, I considered the Municipality of Adjuntas's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing my opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over financial reporting and its operation that I consider to be material weaknesses.

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL (CONTINUED):

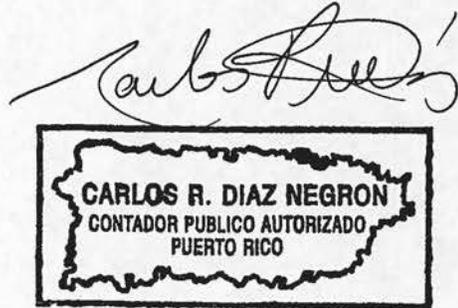
Compliance

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

This report is intended solely for the information and use of the management and the Municipal Legislative Body of Municipality of Adjuntas, federal awarding agencies and passed through-entities and is not intended to be and should not be used by anyone other than these specified parties.

December 14, 2006
Aguas Buenas, Puerto Rico

License No. 1339
Expires December 1, 2007



The Stamp No. 2204047 of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

**REPORT ON COMPLIANCE WITH
REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH
OMB CIRCULAR A-133**

Carlos R. Diaz Negrón

Certified Public Accountant

MEMBER:

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**REPORT ON COMPLIANCE WITH
REQUIREMENT APPLICABLE TO EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

**To the Honorable Mayor and
Municipal Legislative Body
Municipality of Adjuntas
Adjuntas, Puerto Rico**

Compliance

I have audited the compliance of the **Municipality of Adjuntas, Puerto Rico**, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2005. Municipality of Adjuntas, Puerto Rico's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of finding and questioned costs. Compliance with the requirement of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Municipality of Adjuntas, Puerto Rico's management. My responsibility is to express an opinion on the Municipality of Adjuntas, Puerto Rico's compliance based on my audit. The Municipality of Adjunta's basic financial statements include the operations of the Valle Verde Project (a business type activity), which expensed \$2,070,433 in federal awards is not included in the schedule during the year ended June 30, 2005. My audit described below did not include the operations of the Valle Verde Project because those statements were audited by other auditors.

I conducted my audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of State and Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that I plan and perform the audit to obtain reasonable assurance about whether non-compliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Municipality of Adjuntas, Puerto Rico's compliance with those requirements and performing such other procedures as we considered necessary in the circumstance. I believe that my audit provides a reasonable basis for my opinion. My audit does not provide a legal determination on Municipality of Adjuntas, Puerto Rico's compliance with those requirements.

REPORT ON COMPLIANCE WITH REQUIREMENT APPLICABLE (CONTINUED):

As described in the accompanying schedule of findings and questioned cost, the Municipality of Adjuntas did not comply with the followings requirements:

<u>FINDINGS</u>	<u>CFDA NO.</u>	<u>PROGRAM</u>	<u>COMPLIANCE REQUIREMENT</u>
01-06	14.871	Housing Choice Voucher	Special Test and Provisions Eligibility
02-06	14.228	Community Development Block Grant/State Grant	Davis Bacon Act

Compliance with such requirements is necessary in our opinion for Municipality of Adjuntas to comply with the requirements applicable to that program.

In my opinion, Municipality of Adjuntas, Puerto Rico, complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal program for the year ended June 30, 2006.

Internal Control Over Compliance

The management of Municipality of Adjuntas, Puerto Rico is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing my audit, I considered the Municipality of Adjuntas, Puerto Rico's internal control over compliance with requirement that could have a direct and material effect on a major federal program in order to determine my auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

My consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over compliance and its operation that I consider to be material weaknesses.

This report is intended solely for the information and use of the management and the Municipal Legislative Body of the Municipality of Adjuntas, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



December 14, 2006
Aguas Buenas, Puerto Rico

License No. 1339
Expire December 1, 2007

The Stamp No. 2204048 of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2006

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2006**

SECTION I. - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued

Unqualified

Internal control over financial reporting:

- Material weakness (es) identified? ___yes Xno
- Reportable condition (s) identified that are not considered to be material weaknesses? ___yes Xno

Noncompliance material to financial statement noted? ___yes Xno

Federal Awards

Internal control over major programs:

- Material weakness (es) identified? ___yes Xno
- Report condition (s) identified that are not considered to be material weakness(es) ___yes Xno

Type of auditor's report issued on compliance for major programs

Qualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-1331 ___X yes ___no

Identification of major programs:

CFA Number(s)

Name of Federal Program

14.871
14.228

Section 8 – Housing Choice Voucher
Community Development Block
Grants/State's Program

Dollar threshold used to distinguish between type A
And type B programs:

\$300,000

Audit qualified as low-risk audited? ___X yes ___no

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

SECTION II. – FINANCIAL STATEMENTS FINDING

NONE

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

SECTION III. - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 01-06 – Section 8

Federal program

CFDA No. 14.871 – Housing Choice Voucher

Compliance requirement:

Eligibility
Special tests and provisions

Category

Compliance

Condition

As part of any audit procedures I select 5 (five) participants file to test the eligibility and special test and provision requirements of the Housing Choice Voucher Program and the following exceptions were noted:

	<u>Exceptions</u>
No documentation about verification of value of assets.	1
No documentation about the use of comparables unit to determine the reasonableness of the rent.	1
No re-inspection performed in other to ascertain that failures were fixed.	1
New admission not selected from the waiting list in accordance with the PHA selection policies.	1
The PHA does not maintain updated the utility allowance schedule.	

Criteria:

24 CFR Section 982.516 establishes that PHA must: for both family income examinations, obtain and document in the family file third party verification of: (1) reported family annual income, (2) the value of assets, (3) expenses related to deductions from annual income and (4) others factors that affect the determination of adjusted income or income based rent.

**MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

SECTION III. - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS (CONTINUED)

Finding No. 01-06 – Eligibility Test – Section 8 (Continued)

24 CFR Section 982.507 (b) established that PHA must determine whether the rent to owner is reasonable in comparison to rent for other comparable unassisted units. To make this determination. The PHA must consider:

- 1) The location, quality, size unit type, and age of contract unit.
- 2) Any amenities, housing services, maintenance and utilities to be provided by the owner in accordance with the lease.

24 CFR Sections 982.158 (d) and 982.404 establish that for the units under HAP contract that fail to meet Housing Quality Standard (HQS), the PHA must require the owner to correct any life threatening HQS deficiencies within 24 hours after the inspections and all other HQS deficiencies within 30 calendar days or within a specified PHA-approved extension. If the owner does not correct the cited HQS deficiencies within the specified correction period, the PHA must stop (abate) HAPs beginning no later than the first of the month following the specified correction period or must terminate the HAP contract. The owner is not responsible for a breach of HQS as a result of the family's failure to pay for utilities for which the family is responsible under the lease or for tenant damage. For family-caused defects, if the family does not correct the cited HQS deficiencies within the specified correction period, the PHA must take prompt and vigorous action to enforce the family obligation.

24 CFR Section 982.517 (4) (c) establishes that PHA must review its schedule of utility allowances each year, and must revise its allowance for a utility category if there PHAs been a change of 10 percent or more in the utility rate.

24 CFR Section 982.204 (a) and (b) established that except for special admissions, participants must be selected from the PHA waiting list. The PHA must select participants from the waiting list in accordance with admission policies in the PHA administrative plan. The PHA must maintain information that permits the PHA to select participants from the waiting list in accordance with the PHA admission policies. The waiting list must contain the following information for each applicant listed:

- (1) Applicant name;
- (2) Family unit size (number of bedrooms for which family qualifies under PHA occupancy standards);
- (3) Date and time of application;
- (4) Qualification for any local preference;
- (5) Racial or ethnic designation of the head of household.

**MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

SECTION III. - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS (CONTINUED)

Finding No. 01-06 – Section 8

(6) Removing applicant names from the waiting list. (1) The PHA administrative plan must state PHA policy on when applicant names may be removed from the waiting list. The policy may provide that the PHA will remove names of applicants who do not respond to PHA requests for information or updates.

Effect:

The continue occurrence of the condition may result in the disallowance of program cost. In addition, the ability to manage federal awards in compliance with laws, regulations and provision of contracts grant awards could also questioned.

Questioned costs:

None

Recommendation:

I recommend that the Municipality establishes an adequate internal control system to ascertain compliance with the requirements of the program. The internal control system should include at least that file should be revised the internal audit department.

**MUNICIPALITY OF ADJUNTAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2006**

SECTION III. - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

Finding No. 02-06 – Davis-Bacon Act

Federal Program

CFDA – 14.228 – Community Development Block Grant/State's Grant

Compliance requirement:

Davis-Bacon Act

Category:

Compliance

Condition:

As part of my audit procedures I tested 11 (eleven) disbursements to test the compliance with the Davis-Bacon Act for Community Development Block Grant. In 1 (one) disbursement amounting \$182,513.25 of a construction project I do not found the required documents. No copy of the payroll and statement of compliance were found.

Criteria:

The Davis-Bacon Act requires that all construction contracts in excess of \$2,000 financed by federal assistance funds must be paid wages not less than those established for the locality of the project.

Effects:

The Municipality could be exposed to administrative action by the grantor.

Questioned costs:

None

Recommendation:

I recommend that the Municipality establishes an adequate internal control system to ascertain compliance with the Davis-Bacon Act.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ADJUNTAS**

EXHIBIT - I

CORRECTIVE ACTION PLAN

FOR THE YEAR ENDED JUNE 30, 2006

Section 8 Corrective Action Plan

Municipality of Adjuntas

Prepared February 2007

FINDING NO. 01-06-Section 8

Program Deficiency	Objectives	Key Tasks Action Items	Obstacles	Resources	Lead Staff	Completion Target Date	Actual Completion Date	Implementation Progress/Comments
A. The PHA does not keep documentation about verification of value of assets.	1. Update written procedures.	Obtain any information or document to verify that value assets.	None		Coordinator program.	March 31, 2007		
B. The PHA does not keep documentation about the use of comparables unit to determine the reasonableness of the rent.	1. Up dated written procedures and apply these policy and written procedures.	Develop a strategic plan to obtain comparables with all required data. Obtain an adequate number of comparable units. Use and analyze the comparable for each reasonable rent determination.	None		Coordinator program		Done	

Municipality of Adjuntas

Corrective Action Plan

<p>C. Documentation of re-inspection performed in other to ascertain that failures were fixed.</p>	<p>1. Update written procedures. 2. The PHA must re-inspect the unit leased to assure the failures were fixed.</p>	<p>Establish supervision and quality control measures.</p>	<p>None</p>	<p>HCV Guidebook</p>	<p>Director & coordinator program</p>	<p>March 31, 2007</p>				
			<p>None</p>							
<p>D. The PHA does not select from waiting list in accordance with the PHA selection policies.</p>	<p>1. Update written procedures. 2. Prepare the waiting list according to the priorities and preference order.</p>	<p>Establish supervision and quality control measures. Keep the waiting list manageable without creating a management burden.</p>	<p>None</p>							
			<p>None</p>							
<p>E. The PHA does not maintain updated the utility allowance schedule.</p>	<p>1. Compliance and maintain on file information supporting it annual review.</p>	<p>Establish utility allowance control file for all correspondence and other documentation. Clearly show rate increase and calculations.</p>	<p>None</p>							

Municipality of Adjuntas

Corrective Action Plan

FINDING NO. 01-06 Section 8

Program Deficiency	Objectives	Key Tasks/Action Items	Obstacles	Resources	Lead Staff	Completion Target Date	Actual Completion Date	Implementation Progress/ Comments
1. PHA must select participants from waiting list in accordance with admission policies in the PHA administrative plan.	The waiting list must contain the relevant information as: applicant name, family unit size, date & time application, qualification for any local preference and racial or ethnic designation.		None	HCV Guidebook	Coordinator program		Done	

FINDING NO. 01-06 Section 8

Program Deficiency	Objectives	Key Tasks/Action Items	Obstacles	Resources	Lead Staff	Completion Target Date	Actual Completion Date	Implementation Progress/ Comments
2. Removing applicant name from waiting list	State PHA policy on when applicant name may be removed from the waiting list.	Updated Administrative plan or written procedure as needed. Conduct comprehensive review and updated of work-flows and procedures.	None	1. Code of Federal Regulation 24	Director & Consultant	May 31, 2007		

Municipality of Adjuntas

Corrective Action Plan

FINDING NO. O2-06 Community Development Block Grant

Program Deficiency	Objectives	Key Tasks/Action Items	Obstacles	Resources	Lead Staff	Completion Target Date	Actual Completion Date	Implementation Progress/ Comments
Disbursement of federal fund to a construction project without required document.	Obtain all document related with the payroll paid to employees that working on construction project over \$2,000 financed with federal fund.	Request copy of weekly payroll to construction manager's project and verify the wages will be pay not less that those established for the locality of the project.	None	David Bacon Act.	Federal Director	None	None	There not construction in process