

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

MUNICIPIO DE AGUADILLA
AUDITORIA 2002-2003
30 DE JUNIO DE 2003

MUNICIPALITY OF AGUADILLA, PUERTO RICO

SINGLE AUDIT REPORT

FISCAL YEAR ENDED JUNE 30, 2003

MUNICIPALITY OF AGUADILLA, PUERTO RICO

SINGLE AUDIT REPORT

FISCAL YEAR ENDED JUNE 30, 2003

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MUNICIPALITY OF AGUADILLA, PUERTO RICO

FINANCIAL SECTION

YEAR ENDED JUNE 30, 2003



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ROMAN TORO & CO., CSP
Certified Public Accountants and Business Consultants

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

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INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and Members of the
Municipal Assembly
Municipality of Aguadilla, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of **Municipality of Aguadilla, Puerto Rico**, as of and for the year ended June 30, 2003, which collectively comprise the Municipality of Aguadilla, Puerto Rico's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Municipality of Aguadilla, Puerto Rico's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Aguadilla, Puerto Rico, as of June 30, 2003, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 12, 2003, on our consideration of the Municipality of Aguadilla, Puerto Rico's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages 3 through 8 and 39 through 40, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

INDEPENDENT AUDITOR'S REPORT

(CONTINUED)

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Aguadilla, Puerto Rico 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 Municipality of Aguadilla, Puerto Rico. 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.


ROMAN TORO & CO., CSP
LICENSE #35 - IN FORCE

Yauco, Puerto Rico
December 12, 2003

Stamp #1904915 was affixed to
the original of this report

MUNICIPALITY OF AGUADILLA, PUERTO RICO

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

Management of the **Municipality of Aguadilla, Puerto Rico (Municipality)** discussion and analysis is designed to (a) assist the reader in focusing on significant financial issues, (b) provide an overview of the **Municipality's** financial activity, (c) identify changes in the **Municipality's** financial position (its ability to address the next and subsequent year challenges), (d) identify any material deviations from the financial plan (the approved budget), and (e) identify individual fund issues or concerns. This narrative overview and analysis of the financial activities of the **Municipality** is for the fiscal year ended June 30, 2003. We encourage readers to consider this information with the **Municipality's** basic financial statements that follow.

Because the **Municipality** is implementing new reporting standards for this fiscal year with significant changes in content and structure, the Management's Discussion and Analysis (MD&A) is designed to focus on the current year activities, resulting changes and currently known facts, and much of the information is not easily comparable to prior years. However, in future years, comparisons will be more meaningful and will go further in explaining the **Municipality's** financial position and results of operations.

FINANCIAL HIGHLIGHTS

Government-wide:

The **Municipality's** net assets increased by \$3.3 million (or 7.5%).

The governmental activities revenue increased \$3.5 million (or 9%).

Fund Level:

The total cost of all **Municipality** programs decreased by \$8.5 million (or 16%).

The General Fund (the primary operating fund) reflected on a current financial resource basis, reports an increase in fund balance of \$2.6 million.

USING THIS ANNUAL REPORT

This annual report consists of three components: 1) Management's Discussion and Analysis (this section), 2) Basic Financial Statements, and 3) Required Supplementary Information. In light of the fact that this is a very different presentation from the pre-GASB Statement Number 34 model, the following graphic is provided for your review (**Figure A-1** on next page). The Basic Financial Statements include two kinds of statements that present different views of the **Municipality** as follow:

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS, Continued
FOR THE FISCAL YEAR ENDED JUNE 30, 2003**

Government-wide Statements (Reporting the Municipality as Whole)

The **Statement of Net Assets** and **Statement of Activities** are two financial statements that report information about the **Municipality**, as a whole, and about its activities similar to a private-sector business. These statements provide both short-term and long-term information about the **Municipality's** economic condition at the end of the fiscal year. These statements include all assets and liabilities using the accrual basis of accounting. The current year's revenues and expenses are taken into account regardless of when cash is received or paid. The government-wide financial statements include two statements:

The **Statement of Net Assets** (page 10) presents all the **Municipality's** assets and liabilities, with the difference between the two reported as "net assets". Over time, increases and decreases in net assets is an indicator of whether the **Municipality's** financial position is improving or deteriorating.

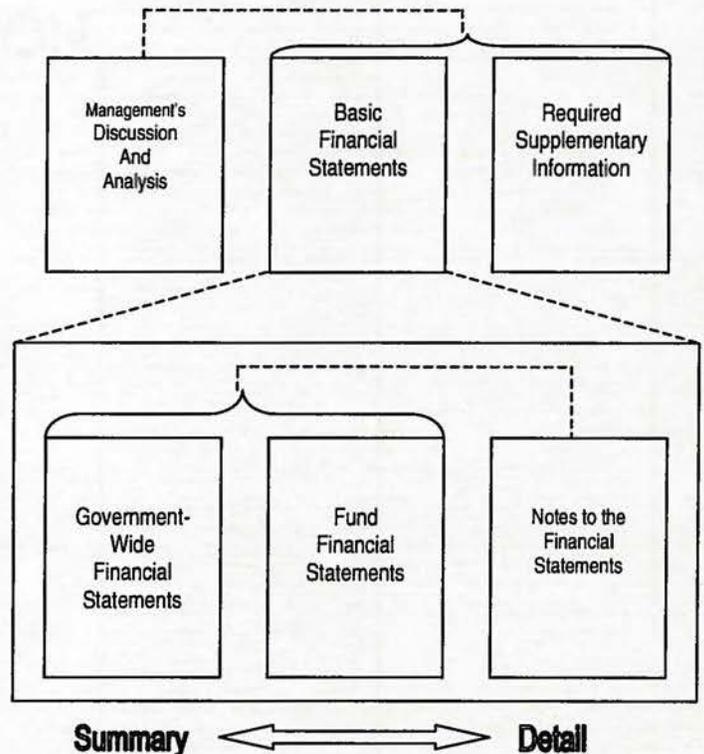
The **Statement of Activities** (page 11) presents information showing how the **Municipality's** net assets change during the most recent fiscal year. All the changes in net assets are reported as soon as the underlying events giving rise to the change occur, regardless of the timing of related cash flows. Therefore, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Fund Financial Statements (Reporting the Municipality's Major Funds)

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is on Major Funds, rather than (the previous financial reporting model's) fund types. The Major Fund presentation is presented on a sources and uses of liquid resources basis. This is the manner in which the financial plan (the budget) is typically developed. The fund financial statements begin on page 12 and provide detailed information about the Major Individual Funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts the **Municipality** uses to keep track of specific sources of funding and spending for a particular purpose. The **Municipality's** funds are all included in Governmental Funds.

The flow and availability of liquid resources is a clear and appropriate focus of any analysis of a government. Funds are established for various purposes and the Fund Financial Statements allows the demonstration of sources and uses and/or budgeting compliance associated therewith (beginning on page 14).

**Figure A-1
Required Component of
Municipality of Aguadilla Annual Financial Report**



MUNICIPALITY OF AGUADILLA, PUERTO RICO

MANAGEMENT'S DISCUSSION AND ANALYSIS, Continued

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

Governmental Funds – the entire **Municipality's** basic service are reported in the governmental funds, which focus in how money flows into out of those funds and the balances left at year-end that are available for future spending. Consequently, the governmental fund financial statements provide a detailed short-term view of the **Municipality** general information, general operation and the basis service it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the **Municipality's** programs.

These funds are reported using modified accrual basis of accounting, which measures cash and all other financial assets that can readily be converted to cash. Under this method, revenues are recognized when measurable and available. Expenditures and generally recognized when the related fund liability is incurred. This is the manner in which these funds are normally budgeted.

Since the governmental fund statements (current financial resources) are presented on a different measurement focus and basis of accounting than governmental-wide statements (total economic resources), a reconciliation of the differences are reflected on the page following each statement (see pages 13 and 15). The flow of current financial resources will reflect bond proceeds and interfund transfers as other financing sources as well as capital expenditures and bond principal payments as expenditures. The reconciliation will eliminate these transactions and incorporate the capital assets and long-term obligation (bonds and others) into the Governmental Activities column (in the Government-Wide Statements).

Infrastructure Assets

Historically, a government's largest group of assets [infrastructure – roads, bridges, traffic signals, underground pipes (unless associated with a utility), etc.] have not been reported nor depreciated in governmental financial statements. GASB Statement Number 34 requires that these assets be valued and reported within the Governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the alternative method), which periodically (at least every third year), by category, measures and demonstrates its maintenance of locally established condition levels, the government may record all expenditures incurred (except for additions and improvements which extend the asset life) in lieu of depreciation. While the **Municipality** has acquired an asset management system which a) would allow the election to use the alternative methods, and b) will provide valuable management information, the Municipality has elected to initially implement the depreciation method, and will monitor and consider, over time, a possible conversion to the alternative method.

Capital Assets Investments

Municipality realized capital assets additions of \$4.5 millions and recognized depreciation expenses in the amount of \$2.0 millions. Principal investments consist of urban development, streets improvement, new buildings, motor vehicles and machinery and equipment acquisitions. Total Investment in Capital Assets, Net of related debt, is \$41.5 millions of 60% of total investment (net of depreciation). Municipality is in process to capitalize all infrastructures in order to be included on or before the fiscal year 2005-2006.

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS, Continued
FOR THE FISCAL YEAR ENDED JUNE 30, 2003**

FINANCIAL ANALYSIS OF THE GOVERNMENT AS A WHOLE

Summary of Net Assets

The Municipality's net assets increase by \$3.9 million over the course of this year's operations. The Municipality's Net Assets include investment in Capital Assets for \$41.5 millions and \$14.8 millions restricted for future expenses. The Municipality's net assets at the end of the fiscal year ended on June 30, 2003 were \$56.3 millions, as detailed on Table 1. For more detailed information see the Statement of Net Assets on page 10.

Normal Impacts

There are six basic (normal) transactions that will affect the comparability of the Net Assets summary presentation.

- **Net Results of Activities** – This will impact (increase/decrease) current assets and unrestricted net assets.

- **Borrowing for Capital** – This will increase current assets and long-term debts.

Current and non-current assets.....	\$ 43,927,280
Capital assets.....	69,359,949
Total Assets.....	<u>113,287,229</u>
Current liabilities.....	10,719,554
Long-term liabilities.....	45,170,755
Total Liabilities.....	<u>55,890,309</u>
Nets Assets:	
Investment in capital assets.....	39,924,949
Restricted.....	14,826,947
Unrestricted.....	2,645,023
Total Net Assets.....	<u>\$ 57,396,919</u>

- **Spending Borrowed Proceeds on New Capital** – This will reduce current assets and increase capital assets. There is a second impact, an increase in invested in capital assets and an increase in related net debt which will not change the invested in capital assets, net of debt.
- **Spending of Non-borrowed Current Assets on New Capital** – This will (a) reduce current assets and increase capital assets and (b) reduce unrestricted net assets and increase invested in capital assets, net of debt.
- **Principal Payment on Debt** – This will (a) reduce current assets and reduce long-term and (b) reduce unrestricted net assets and increase invested in capital assets, net of debt.
- **Reduction of Capital Assets through Depreciation** – This will reduce capital assets and invested in capital assets, net of debt.

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS, Continued
FOR THE FISCAL YEAR ENDED JUNE 30, 2003**

Current Year Impacts

The following schedule (as detailed on **Table 2**) presents the revenues and expenses for the current fiscal year.

Table 2	
Changes in Net Assets	
For Fiscal Year Ending June 30, 2003	
Revenues:	
Program Revenues:	
Charges for Services	\$ 1,506,326
Federal Grants and Contributions.....	10,069,380
State Grants and Contributions.....	1,636,661
General Revenues:	
Property Taxes.....	10,921,637
Volume of Business Taxes	9,275,555
Construction Taxes.....	851,182
Intergovernmental.....	5,015,103
Other General Revenues.....	1,082,427
Gain on Sale of Assets	1,332,408
Total revenues	<u>41,690,679</u>
Expenses:	
General Administration	13,586,125
Public Safety	1,593,075
Public Works	1,852,132
Health and Sanitation.....	2,751,255
Culture and Recreation	1,750,877
Solid Waste Disposal	800,000
Human Services and Welfare	4,273,982
Urban Development.....	4,075,892
Education.....	6,048,666
Interest Costs.....	1,665,337
Total expenses	<u>38,397,341</u>
Changes in net assets	3,293,338
Net assets – beginning	<u>54,103,581</u>
Net assets – ending	<u>\$ 57,396,919</u>

Normal Impacts

There are seven impacts on revenues and expenses as reflected below.

Revenues:

Economic Condition – which can reflect a declining, stable or growing economic environment and has substantial impact on property and volume of business tax revenues as well as public spending habits for building permits, elective user fees and volumes of consumption.

Increase/Decrease in Municipality Approved Rates – while certain tax rates are set by stature, the **Municipality** has significant authority to impose and periodically increase/decrease rates.

Changing Patterns in Intergovernmental and Grant Revenue (both recurring and non-recurring) – certain recurring revenues (states revenue sharing, block grants, etc.) may experience significant changes periodically while non-recurring (or one-time) grants are less predictable and often distorting in their impact on year revenues.

Expenses:

Introduction of New Programs – within the functional expense categories individual programs may be added or deleted to meet changing community needs.

Increase/Decrease in Authorized Personnel – changes in service demand may cause the **Municipality** to increase/decrease authorized staffing. Staffing costs (salary and related benefits) represent 45% of the **Municipality's** operating cost.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS, continued
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

Salary Increases (cost of living, merit and market adjustment) – the ability to attract and retain human and intellectual resources requires the **Municipality** to strive to approach a competitive salary range position in the marketplace. Salaries increase of \$50 monthly is expected for the next fiscal year.

Inflation – while overall inflation appears to be reasonably modest, the **Municipality** is a major consumer of certain commodities such as chemicals and supplies, fuels and parts. Some functions may experience unusual commodity specific increases.

Current Year Impacts

Revenues:

Property Taxes which appear flat was actually a result of a declining, stable or growing economic environment and has substantial impact on property and volume of business tax revenues as well as public spending habits for building permits, elective user fees and volumes of consumption.

Charges for Services was primarily for the use of Water Theme Park Las Cascadas and collection from solid waste disposal in municipal landfill for the amounts of \$1.3 million and \$243,000, respectively.

Intergovernmental Revenues which appear flat was actually a result of a declining, stable or growing economic environment and has substantial impact on property and volume of business tax revenues as well as public spending habits for building permits, elective user fees and volumes of consumption.

Expenses:

Introduction of New Programs – within the functional expense categories individual programs may be added or deleted to meet changing community needs.

Increase/Decrease in Authorized Personnel – changes in service demand may cause the **Municipality** to increase/decrease authorized staffing. Staffing costs (salary and related benefits) represent 44% of the **Municipality's** operating cost.

Net Assets:

Net Assets reflect an increase of \$3,293,338 corresponding to an increase in revenues over expenses.

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

As the **Municipality's** completed the year, its governmental funds reported fund balances of \$2.8 millions. Of this total amount, \$1.5 or 54% constitute unreserved fund balance, which is available for appropriation for the general purposes of the programs administer by the **Municipality**.

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS, Continued
FOR THE FISCAL YEAR ENDED JUNE 30, 2003**

General Fund Budgetary Highlights:

The total budget for the **Municipality** was \$25.8 millions and actual spending was \$24.4 millions. Total expenditures represented 95% of total budget availability for the period. Current year budgetary fund balance was positive in the amount of \$2.7 millions corresponding to an increase in revenues of \$1.3 million and economies in appropriations of \$1.4 million.

Economic Factors and Next Year's Budgets

For the fiscal year 2002-03, the **Municipality** actual revenues are \$27.1 millions, exceeding the budget amount for \$1.3 millions.

CONTACTING THE MUNICIPALITY'S OFFICE OF FINANCIAL MANAGEMENT

This report is designed to provide a general overview of the **Municipality's** finances and to demonstrate the accountability for the money it receives. If you have any questions about this report or need additional information, contact the **Municipality's** Finance Department at (787) 891-1005, Extension 3046.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

STATEMENT OF NET ASSETS

JUNE 30, 2003

	<u>GOVERNMENTAL ACTIVITIES</u>
ASSETS:	
Cash and Investments	\$ 28,628,884
Cash with Fiscal Agent	8,251,577
Receivables (net):	
Federal Grants	6,865,341
Volume of Business Tax	32,215
Others	<u>149,264</u>
Capital Assets (Note 1):	
Land, Improvements, and Construction in Progress	22,544,875
Other Capital Assets, [Net of Depreciation].....	<u>46,815,074</u>
Total Capital Assets	<u>69,359,949</u>
TOTAL ASSETS	<u>113,287,229</u>
LIABILITIES:	
Accounts Payable and Accrued Expenses	\$ 3,260,507
Accrued Interest.....	993,983
Deferred Revenue.....	6,465,064
Long-Term Liabilities (Note 2):	
Due within One Year	5,535,436
Due in More than One Year.....	<u>39,635,319</u>
Total Liabilities	<u>55,890,309</u>
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	39,924,949
Restricted for:	
Capital Projects	1,138,918
Head Start Program	3,661,611
Debt Service.....	2,015,826
Community Development Projects	3,819,617
Other Purposes	4,190,975
Unrestricted.....	<u>2,645,023</u>
TOTAL NET ASSETS	<u>\$ 57,396,919</u>

See accompanying Notes to Basic Financial Statements.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

STATEMENT OF ACTIVITIES

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

FUNCTIONS/PROGRAMS	EXPENSES	PROGRAM REVENUES			NET (EXPENSE) REVENUE (SEE NEXT PAGE)
		CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS	
Governmental Activities:					
Mayor and Municipal Legislature.....	\$ 2,612,215	\$ -	\$ -	\$ -	\$ (2,612,215)
General Government.....	10,973,910	-	1,393,293	-	(9,580,617)
Public Safety	1,593,075	-	-	-	(1,593,075)
Public Works	1,852,132	-	-	-	(1,852,132)
Health and Sanitation	2,751,255	-	-	-	(2,751,255)
Culture and Recreation	1,750,877	1,262,959	-	-	(487,918)
Solid Waste Disposal	800,000	243,367	-	-	(556,633)
Human Services and Welfare.....	4,273,982	-	1,597,432	-	(2,676,550)
Urban Development	4,075,892	-	3,109,675	-	(966,217)
Education	6,048,666	-	5,605,641	-	(443,025)
Interest on Long-Term Debt	1,665,337	-	-	-	(1,665,337)
Total Governmental Activities.....	\$ 38,397,341	\$ 1,506,327	\$ 11,706,041	\$ -	(25,184,974)

General Revenues:

Taxes:

Volume of business taxes.....	9,275,555
Property Taxes, levied for General Purposes.....	8,705,931
Property Taxes, levied for Debt Service	2,215,706
Construction taxes.....	851,182
Intergovernmental	5,015,103
Rent.....	259,120
Miscellaneous.....	823,309
Special Item – Gain on Sale.....	1,332,408

Total General Revenues and Special Items..... 28,478,312

CHANGE IN NET ASSETS..... 3,293,338

Net Assets – Beginning of Year

54,103,581

NET ASSETS – ENDING OF YEAR..... \$ 57,396,919

See accompanying Notes to Basic Financial Statements.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

BALANCE SHEET – GOVERNMENTAL FUNDS

JUNE 30, 2003

	<u>GENERAL</u>	<u>HEAD START FUND</u>	<u>DEBT SERVICE FUND</u>	<u>PASEO REAL MARINA FUND</u>	<u>CDBG FUND</u>	<u>OTHER GOVERNMENTAL FUNDS</u>	<u>TOTAL GOVERNMENTAL FUNDS</u>
ASSETS							
Cash and Investments (Note 1).....	\$ 9,840,849	\$ 39,289	\$ -	\$ 12,936,802	\$ 225,128	\$ 5,586,816	\$ 28,628,884
Cash with Fiscal Agent	-	-	4,276,511	-	-	3,975,066	8,251,577
Receivables:							
Federal Grants	-	3,681,642	-	-	2,716,628	467,070	6,865,340
Due from Other Funds	173,430	-	-	-	-	-	173,430
Volume of Business Tax	32,215	-	-	-	-	-	32,215
Others	<u>38,062</u>	-	-	-	-	<u>111,202</u>	<u>149,264</u>
TOTAL ASSETS	<u>\$ 10,084,556</u>	<u>\$ 3,720,931</u>	<u>\$ 4,276,511</u>	<u>\$ 12,936,802</u>	<u>\$ 2,941,756</u>	<u>\$ 10,140,154</u>	<u>\$ 44,100,710</u>
LIABILITIES AND FUND BALANCES							
Liabilities:							
Accounts Payable	\$ 857,553	\$ 59,321	\$ 1,550,000	\$ -	\$ 149,389	\$ 427,270	\$ 3,043,533
Accrued Interest	-	-	710,685	283,298	-	-	993,983
Due to Governmental Units	80,617	-	-	-	-	-	80,617
Due to Other Funds	-	-	-	-	11,658	161,772	173,430
Others	136,357	-	-	-	-	-	136,357
Deferred Revenues:							
Volume of Business Tax	6,218,910	-	-	-	-	-	6,218,910
Local Grants	-	-	-	-	-	113,166	113,166
Federal Grants	-	<u>3,622,321</u>	-	-	<u>2,716,628</u>	<u>132,988</u>	<u>6,471,937</u>
Total Liabilities (Note 2)	<u>7,293,437</u>	<u>3,681,642</u>	<u>2,260,685</u>	<u>283,298</u>	<u>2,877,675</u>	<u>835,196</u>	<u>17,231,933</u>
Fund Balances:							
Reserve For:							
Encumbrances	1,252,968	-	-	-	-	-	1,252,968
Debt Service	-	-	2,015,826	-	-	-	2,015,826
Other Purposes	-	39,289	-	12,653,504	64,081	9,304,958	22,061,832
Unreserved	<u>1,538,151</u>	-	-	-	-	-	<u>1,538,151</u>
Total Fund Balances	<u>2,791,119</u>	<u>39,289</u>	<u>2,015,826</u>	<u>12,653,504</u>	<u>64,081</u>	<u>9,304,958</u>	<u>26,868,777</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 10,084,556</u>	<u>\$ 3,720,931</u>	<u>\$ 4,276,511</u>	<u>\$ 12,936,802</u>	<u>\$ 2,941,756</u>	<u>\$ 10,140,154</u>	<u>\$ 44,100,710</u>

Continue

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
BALANCE SHEET – GOVERNMENTAL FUNDS, Continued
JUNE 30, 2003**

**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS**

Total Fund Balances – Governmental Funds (Page 12)..... \$ 26,868,777

Amounts reported for Governmental Activities in the Statement of Net Assets (Page 11)
are different because:

Capital Assets used in governmental activities are not financial resources and therefore are
not reported in the funds. In the current period, these amounts are:

Non Depreciable Capital Assets.....	\$ 22,544,875	
Depreciable Capital Assets.....	64,636,760	
Infrastructure Assets.....	9,095,160	
Accumulated Depreciation.....	<u>(26,916,848)</u>	
Total Capital Assets.....		69,359,947

Some of the **Municipality's** revenues will be collected after year-end but are not available
soon enough to pay for the current period's expenditures and therefore are deferred in
the funds:

Head Start	3,622,322	
CDBG	<u>2,716,628</u>	
Total Deferred Revenues.....		6,338,950

Some liabilities are not due and payable in the current period and therefore are not reported
in the funds. Those liabilities consist of:

General Bonds and Notes Payable	40,880,000	
Compensated Absences	2,864,597	
Claims and judgement	500,000	
Landfil Closure and Postclosure Costs.....	800,000	
Property Tax Advances	<u>126,158</u>	
Total Long-Term Liabilities		<u>(45,170,755)</u>

Total Net Assets of Governmental Activities (Page 10)..... \$ 57,396,919

See accompanying Notes to Basic Financial Statements.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE –
GOVERNMENTAL FUNDS**

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

	<u>GENERAL</u>	<u>HEAD START FUND</u>	<u>DEBT SERVICE FUND</u>	<u>PASEO REAL MARINA FUND</u>	<u>CDBG FUND</u>	<u>OTHER GOVERNMENTAL FUNDS</u>	<u>TOTAL GOVERNMENTAL FUNDS</u>
REVENUES							
Property Taxes	\$ 8,705,931	\$ -	\$ 2,215,706	\$ -	\$ -	\$ -	\$ 10,921,637
Volume of Business Taxes	9,275,555	-	-	-	-	-	9,275,555
Federal Assistances	-	4,758,871	-	-	3,577,910	2,599,444	10,936,225
Intergovernmental	5,015,103	-	-	-	-	1,636,661	6,651,764
Licenses and Permits	851,182	-	-	-	-	-	851,182
Rent	259,120	-	-	-	-	-	259,120
Miscellaneous	823,307	-	-	-	-	1,262,959	2,086,266
Total Revenues	24,930,198	4,758,871	2,215,706	-	3,577,910	5,499,064	40,981,749
EXPENDITURES							
Current:							
Mayor and Municipal Legislature	2,516,709	-	-	-	-	-	2,516,709
General Government	10,510,020	-	-	-	-	889,606	11,399,626
Public Safety	1,510,667	-	-	-	-	-	1,510,667
Public Works	1,535,509	-	-	-	-	-	1,535,509
Health and Sanitation	2,554,144	-	-	-	-	-	2,554,144
Culture and Recreation	937,114	-	-	-	-	769,719	1,706,833
Human Services and Welfare	2,797,821	-	-	-	-	1,865,634	4,663,455
Urban Development	206,529	-	-	58,198	3,516,755	3,115,756	6,897,238
Education	-	5,617,329	-	-	-	-	5,617,329
Capital Outlay	166,757	-	-	-	-	385,098	551,855
Debt Service:							
Principal	-	-	3,330,000	-	-	-	3,330,000
Interest and Other Charges	-	-	1,382,039	283,298	-	-	1,665,337
Total Expenditures	22,735,270	5,617,329	4,712,039	341,496	3,516,755	7,025,813	43,948,702
OTHER FINANCING SOURCES (USES)							
Bonds Issued	-	-	-	12,995,000	-	5,360,000	18,355,000
Transfers – In	-	-	2,009,202	-	-	1,473,144	3,482,346
Transfers – Out	(1,777,346)	-	-	-	-	(1,705,000)	(3,482,346)
Total Other Financing Sources and Uses	(1,777,346)	-	2,009,202	12,995,000	-	5,128,144	18,355,000
SPECIAL ITEM							
Proceeds from Sale of Land	2,189,750	-	-	-	-	-	2,189,750
Net Change in Fund Balances	2,607,332	(858,458)	(487,131)	12,653,504	61,155	3,601,395	17,577,797
Fund Balance – Beginning, as Restated	183,787	897,747	2,502,957	-	2,926	5,703,563	9,290,980
FUND BALANCES – ENDING	\$ 2,791,119	\$ 39,289	\$ 2,015,826	\$ 12,653,504	\$ 64,081	\$ 9,304,958	\$ 26,868,777

Continue

MUNICIPALITY OF AGUADILLA, PUERTO RICO

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE –
GOVERNMENTAL FUNDS, Continued**

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES**

Net Change in Fund Balances – Total Governmental Funds (Page 14)..... \$ 17,577,797

Amounts reported for Governmental Activities in the Statement of Activities (Page 11)
are different because:

Governmental funds report capital outlays as expenditures. However, in the Statement of
Activities the cost of those assets is allocated over their estimated useful lives and reported
as depreciation expense. In the current period, these amounts are:

Urban Development and Capital Outlay	\$ 4,477,490	
Depreciation Expense	(2,041,435)	
Excess of Capital Outlay over Depreciation Expense		2,436,055

In the Statement of Activities, only the gain on the sale of the assets is reported, whereas
in the governmental funds, the proceeds from the sale increase financial resources. Thus,
the change in net assets differs from the change in fund balance by the cost of the assets (857,342)

Revenues in the Statement of Activities that do not provide current financial resources are
not reported as revenues in the funds..... (623,477)

Bonds proceeds provide current financial resources to governmental funds, but issuing debt
Increases Long-Term Liabilities in the Statement of Net Assets. In the current period,
proceeds received was (18,355,000)

Repayment of long-term principal is expenditure in the governmental funds, but the repayment
reduces Long-Term Liabilities in the Statement of Net Assets. In the current year the
repayments were..... 3,330,000

Some expenses reported in the Statement of Activities do not require the use of current
financial resources and therefore are not reported as expenditures in governmental funds.
These activities consist of:

Increase in Compensated Absences	(\$ 51,466)	
Increase in Landfill Closure and Postclosure Cost	(800,000)	
Decrease in Claims and Judgments	500,000	
Decrease in Other Debt	136,771	
Total Additional Expenditures		(214,695)

Change in Net Assets of Governmental Activities (Page 11)..... \$ 3,293,338

See accompanying Notes to Basic Financial Statements.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Aguadilla, Puerto Rico (Municipality) was founded in the year 1775, and operates as a governmental unit of the Commonwealth of Puerto Rico, under the Law Number 81 of August 30, 1991, known as "Autonomy Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the Municipality is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of the Commonwealth of Puerto Rico. The legislative body consists of 14 Legislators also elected in the general elections of Puerto Rico for a four-year period.

The Municipality provides services such as: health, public works, sanitation, aids and services to low-income and elderly citizens, public safety, housing and urban development, culture and recreation, planning, zoning and other general and administrative services.

The accounting policies of the Municipality conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The following is a summary of the more significant of such policies.

The accompanying basic financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). The GASB is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards which, along with subsequent GASB pronouncements (Statements and Interpretations) constitutes GAAP for governmental units.

In June 1999, the GASB issued Statement Number 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*. This statement establishes new financial reporting requirements for state and local governments. The Municipality adopted the provisions of GASBS No. 34 as well as other statements referred to below as of July 1, 2002. They require new information and restructure much of the information that governments have presented in the past.

Comparability with reports issued in prior years is affected. With the implementation of GASBS No. 34, the Municipality has prepared required supplementary information titled Management's Discussion and Analysis, which precedes the basic financial statements.

As previously mentioned, other GASB Statements and Interpretations were required to be implemented in conjunction with GASBS No. 34. Therefore, the Municipality has implemented the following GASB Statements in the current fiscal year: GASBS No. 37, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments: Omnibus*, GASBS No. 38, *Certain Financial Statement Note Disclosures*, and GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

The accompanying basic financial statements present the financial position and the results of operations of the Municipality and its various funds and fund types. The basic financial statements are presented as of June 30, 2003, and for the fiscal year then ended. The more significant of these accounting policies are described below and, where appropriate, subsequent pronouncements will be referenced.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

A. Financial Reporting Entity

The accompanying basic financial statements include all departments and organizations units whose funds are under the custody and control of the Municipality. In evaluating the Municipality as a reporting entity, management has addressed all the potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of GASBS No. 14.

The basic criteria for including a potential component unit within the reporting entity is if potential component units are financially accountable and other organizations for which the nature and significance of their relationship with the entity are such that exclusion would cause the Municipality's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) ability of the Municipality to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Municipality.

The relative importance of each criteria must be evaluated in light of specific circumstances in order to determine which components units are to be included as part of the reporting entity. Our specific evaluations of the criteria applicable to the Municipality indicate no organizations meet the criteria to be included as component units. Accordingly, these basic financial statements present only the Municipality as the reporting entity.

These financial statements present the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2003, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

B. Measurement Focus and Basis of Accounting

Government-wide Financial Statements

The government-wide financial statements (the Statement of Net Assets and the Statement of Activities) are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grant and similar items are recognized as revenue as soon as all eligibility requirements have been met.

Governmental Fund Financial Statements

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recorded when susceptible to accrual; as soon as it is both measurable and available. "Available" means collectible within the current period or soon enough thereafter, normally within sixty (60) days, to be used to pay liabilities of the current period. Expenditures are generally recognized when the related liability is incurred.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

The exception to this general rule is the principal and interest on general obligation long-term debt and compensated absences, if any, are recognized when due.

In applying the "susceptible to accrual" concept to intergovernmental revenues (federal grants) pursuant to GASBS No. 33, *Accounting and Financial Reporting for Nonexchange Transactions* (the Municipality may act as either provider or recipient), the provider should recognize liabilities and expenses and the recipient should recognize receivables and revenue when the applicable eligibility requirements including time requirements, are met. Resources transmitted before the eligibility requirements are met should, under most circumstances, be reported as advances by the provider and deferred revenue by the recipient.

There are essentially two types of revenue. For the majority of grants, moneys must be expended by the Municipality on the specific purpose or project before any amounts will be reimbursed. Revenue is, therefore, recognized as expenditures are incurred to the extent available. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt or earlier if the susceptible to accrual criteria is met.

Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- Employee's vested annual vacation and sick leave is recorded as expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2003, has been reported only in the government-wide financial statements.

C. Financial Statement Presentation

The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements. While the previous financial reporting model emphasized fund types (the total of all funds of a particular type), in the new financial model the focus is on either the Municipality as a whole, or major individual funds (within the basic financial statements). Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as either governmental or business type.

Government-wide Financial Statements

The government-wide financial statements (the Statement of Net Assets and the Statement of Activities) report information of all the activities of the Municipality. For most part, the effect of interfund activity has been removed from these government-wide financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

The focus of the Statement of Net Assets is designed to be similar to bottom line results for the Municipality and its governmental activities. This statement, for the first time, combines and consolidates governmental fund's current financial resources (short-term spendable resources) with capital assets and long-term obligations.

The Statement of Net Assets presents the reporting entities' assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- Invested in Capital Assets, Net of Related Debt – These consists of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- Restricted Net Assets – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- Unrestricted Net Assets – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

The Statement of Activities is focused on both the gross and net costs per functional category. The statement reduces gross expenses (including depreciation) by related program revenues, operating and capital grants. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

Governmental Fund Financial Statements

The fund financial statements (the Balance Sheet, the Statement of Revenues, Expenditures, and Changes in Fund Balances, the Statement of Net Assets) are, in substance, very similar to the financial statements presented in the previous financial reporting model. Emphasis here is on the major funds in the governmental category. Non-major funds are summarized into a single column.

Traditional users of governmental financial statements will find the Fund Financial Statements presentation more familiar. The focus is on Major Funds, rather than the previous financial model's fund types. The Governmental Major Fund Statements are presented on current financial resources and modified accrual basis of accounting.

This is the manner in which these funds are normally budgeted. This presentation deemed most appropriate to (a) demonstrate legal and covenant compliance, (b) demonstrate the source and use of liquid resources, and (c) demonstrate how the Municipality's actual experience conforms to the budgeted fiscal plan.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

Since the governmental fund statements are presented in different measurement focus and basis of accounting than the government-wide statements, reconciliation is presented and separate explanation for each differences.

The Municipality reports its financial position (Balance Sheet) and results of operations (Statement of Revenues, Expenditures and Changes in Fund Balance) in funds, which are considered separate accounting entities. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions.

The new model as defined in GASBS No. 34 established criteria (percentage of the assets, liabilities, revenues, or expenditures/expenses of either fund category in the governmental fund) for the determination of major funds. The non-major funds are combined in a single column in the fund financial statements. The Municipality reports the following major fund:

General Fund – This is the general operating fund of the Municipality. It is used to account for all financial resources, except those required to be accounted for in another fund.

Head Start Fund – This is the fund used to account for all transactions of the Head Start Program. The objectives to this program are to provide comprehensive health, educational, nutritional, social and other developmental services primarily to economically-disadvantaged pre-school children and infants and toddlers so that the children will attain school readiness.

Debt Service Fund – This is used to account for the accumulation of resources for, and the payment of, long-term debt principal and interests.

Paseo Real Marina Fund – This is a capital project fund used to account for all financial resources and transactions related to the construction of the Paseo Real Marina Project, which is financed by a Section 108 Loan from the US Department of Housing and Urban Development (HUD).

CDBG Fund – This is the fund used to account for all the transactions of the Community Development Block Grant Program. The primarily objective of this program is to develop of viable communities by providing decent housing, a suitable living environment and expanded economic opportunities, principally for persons of low and moderate income.

GASBS No. 34 eliminates the presentation of Account Groups, but provides for these records to be maintained and incorporates the information into the Governmental column in the government-wide Statement of Net Assets.

D. Budgetary Data

The Municipality's annually adopts the Budget Resolution for all operating funds of the Municipality except for certain restricted accounts Special Revenue Funds. Budgetary control is legally maintained at the fund level. The budget is prepared using the modified accrual basis of accounting with encumbrance included as budgetary basis expenditures. The Municipality's Budget Resolution provides transfer authority (1) to the Mayor and the Management and Budget Director, within and between departments and funds, as long as the total budget of the Municipality (net of interfund transfers) is not increased; (2) to the Management

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

and Budget Director to implement grant budgets as the grant applications are accepted by the Municipality; and (3) to the Management and Budget Director to amend (re-appropriate) each new year's budget, to the extent of outstanding encumbrances, and/or unexpended project/grant appropriations at year end. Municipality's Legislature action is required for (1) use of the budgeted Legislature contingency, and (2) the approval of a supplemental appropriation(s). During the year, several supplemental appropriations were necessary.

The budget columns (original and final budgets) of the Budgetary Comparison – General Fund reflect the original budget and the amended budget (which have been adjusted for legally authorized revisions of the annual budgets during the year). Appropriations, except remaining project appropriations, encumbrances, and unexpended grant appropriations, lapse at the end of each fiscal year.

Amendments to the budget, including transfers, require the approval of the Municipal Legislature. Unencumbered appropriations lapse at the end of the next fiscal year. The Municipality follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the basic financial statements:

1. Prior of May 31 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message.
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature.
3. The Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law.
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance.
5. If a budget is not adopted prior to the end of the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Municipal Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until a new budget is approved. This permits the Municipality to continue making payments for its operating and other expenses until the new budget is approved.
6. Subsequent to the enactment of the annual appropriation ordinance, the Municipal Legislature has the authority to make necessary amendments made during the fiscal year and are reflected in the budget information included in the Budgetary Comparison Schedule – General Fund.
7. Budgetary data for the Special Revenue Fund has not been presented in the accompanying basic financial statements as such funds are budgeted over the life of the respective grant or project and not on an annual basis.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

Since the budgetary basis differs from accounting principles generally accepted in the United States of America (GAAP), actual amounts for the General Fund in the accompanying Budgetary Comparison Schedule, is presented on the budgetary basis to enhance comparability.

The principal differences between the budgetary and GAAP bases are the following:

1. Encumbrances are recorded as expenditures under the budgetary basis and as a reserve of fund balances under GAAP.
2. The non-exonerated portion of the property tax advances are presented as revenue in the budgetary basis and as other financing sources under GAAP (See Note 10).
3. Interfund transactions of the General and Special Revenue Funds are not included in the budgetary basis.
4. Certain accrued liabilities and other debts are not included in the budgetary basis.
5. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

All encumbrance appropriations in the operating budget lapse at the end of the fiscal year. Property taxes collected during the current year by the Municipal Revenue Collection Center (Fiscal Agent) are presented as revenues in the accounting basis but are not considered in the budgetary schedule.

The special funds of the Special Revenue Fund have not been included in the budgetary comparison because balances are not budgeted. Also the budget prepared for the Federal Financial Awards Programs included in the Capital Projects and Special Revenue Funds is based on a program period which is not necessarily a year. Accordingly, it's not practical to present an annual comparison of budget for such programs.

E. Cash, Cash Equivalent and Investment

The Director of Finance of the Municipality is responsible for investing the available resources in certificates of deposit and other short-term investments. Investments are made from the available combined funds of the Municipality and, accordingly, it is not practical to disclose certificates of deposit and other short-term investments individually by fund in the combined financial statements. Interest earned on certificates of deposit and other short-term investments are recognized as revenue in the General Fund. Cash in the Special Revenue, Debt Service and Capital Project Funds are restricted; accordingly, resources available were not used for pool investments.

Cash with fiscal agent represents property tax collections retained by the Municipal Revenues Collection Center and undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico.

Cash balance recognized in the Debt Service Fund is restricted for the payment of the Municipality's obligations, and others are restricted for specific projects, such as the acquisition or construction of

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

permanent improvements. This sinking fund is maintained by the Governmental Development Bank of Puerto Rico, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

F. Receivable

Receivable are stated nets of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions. Receivable from Federal Government represents amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs.

G. Inventories

The General, Special Revenue and Capital Project Funds, purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. The cost of purchases is recorded as expenditure in the appropriate fund and the inventory is not recorded in the basic financial statements.

H. Capital Assets

Property, plant and equipment purchased or acquired is carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date received. The Municipality's capitalization levels are \$500 on personal property. For improvements other than buildings, the capital outlay must be greater than \$10,000, extend the estimated useful life for ten years, and be greater than 10% of the original cost of the asset. Other costs incurred for repairs and maintenance is expensed as incurred.

Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

<u>CAPITAL ASSETS</u>	<u>YEARS</u>
Buildings	50
Improvement Other Than Buildings	50
Equipment	10
Furniture	10
Vehicles	5
Machinery	5-10
Infrastructure	10-50

I. Compensated Absences

The Municipality accrues accumulated unpaid vacation and sick leave and associated employee-related costs when earned (or estimated to be earned) by the employee. The Municipality's employees are granted 30 days of vacations and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of sixty (60) days and sick leave up to a maximum of ninety (90) days. In the event of employee resignation, the employee is paid for accumulated vacation 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 of service who are entitled to sick leave pay up to the maximum allowed. The Municipality accrued a liability for compensated absences, which meet the following criteria:

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

1. The Municipality's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered.
2. The obligation relates to rights that vest or accumulate.
3. Payment of the compensation is probable.
4. The amount can be reasonably estimated.

In accordance with the above criteria and requirements as established by GASBS No. 16; the Municipality has accrued a liability for compensated absences, which has been earned but not taken by Municipality's employees. For the government-wide statements, the current portion is the amount estimated to be used in the following year. For the governmental funds statements, all of the compensated absences are considered long-term and therefore, are not a fund liability and represents a reconciling item between the fund level and government-wide presentations (see NOTE 6 on page 31).

The following is a summary of changes in the balance of Compensated Absences for the fiscal year ended June 30, 2003.

BALANCE JULY 1, 2002	NEW ISSUES	RETIREMENTS AND CURRENT MATURATES	BALANCE JUNE 30, 2003	CURRENT PORTION	LONG-TERM PORTION
<u>\$2,813,131</u>	<u>\$ 51,466</u>	<u>\$ -</u>	<u>\$2,864,597</u>	<u>\$1,844,597</u>	<u>\$1,020,000</u>

J. Insurance

The Municipality has insurance coverage for its public facilities, primarily to provide protection from catastrophic losses. Also, principal officials of the Municipality are covered under various surety bonds. The Secretary of the Treasury Department of the Commonwealth of Puerto Rico is the agent commissioned to place all of the Municipality's insurance coverage. Corresponding premiums payable are withheld by the Municipal Revenue Collection Center from quarterly advances of annual property tax and subsidy sent to the Municipality.

K. Interfund Transactions

Interfund transactions are reflected as loans, reimbursements or transfers. Loans are reported as receivables and payables as appropriate and are subject to elimination upon consolidation. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the government-wide columnar presentation. The Municipality has the following types of transactions among funds:

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued

Interfund Transfers – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds. Advances between funds are also presented as amounts due to and due from other funds. However, these transfers and related amounts receivables and payables are considered internal balances and activities that have been eliminated in the government-wide financial statements.

L. Reservations of Fund Balance – Governmental Funds

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditures or (2) legally segregated for a specific future use. The reserves for related assets such as inventories and prepayments are examples of the former. Reserves for encumbrances, debt service, and other specific purposes are examples of the latter. The Municipality has the following reservations of fund balance:

Encumbrance – Represent future expenditures under purchases orders, contracts and other commitments issued for goods and services not received at year-end. Where the appropriations lapse at year-end these will be honored during subsequent year. Encumbrances constitute the equivalent of expenditures for budgetary purposes and, accordingly, are reported with expenditures in the budgetary comparison schedule.

Debt Service – Represents net assets available to finance future debt service payments.

M. Claims and Judgments

The estimated amount of the liability for claims and judgments, if any, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund. The Long-Term Debt Account includes an amount estimated as a contingent liability or liabilities with a fixed or expected due date, which will require future available financial resources for its payment.

N. Use of Estimates

The preparation of the basic 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 disclosures of contingent assets and liabilities at the date of the basic financial statements and the reported revenue and expenses during the reporting period. Actual result could differ from those estimates.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 2 CASH, CASH EQUIVALENTS AND INVESTMENTS

Investments consist of certificates of deposit. The Municipality's cash, cash equivalent and investments at year-end were entirely covered by the Federal Deposit Insurance Corporation (FDIC) coverage, up to a maximum of \$100,000 in each bank, and the excess by collateral provided by the banks and held by the Department of the Treasury pursuant the applicable laws and regulations. Cash with fiscal agent is maintained in interest bearing accounts in the Government Development Bank of Puerto Rico and is not collateralized.

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Commonwealth of Puerto Rico. The Municipality is also allowed to invest in bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the federal and Commonwealth laws.

During the year, the Municipality invested its funds in interest bearing bank accounts and short-term certificates of deposit. As June 30, 2003, the market value of investments recorded in Special Revenue Fund approximated its carrying value as follow:

Certificate OF DEPOSIT ISSUED BY	PRINCIPAL NUMBER	INTEREST AMOUNT	RATE	EXPIRATION DATE
Popular Bank of Puerto Rico	1110000118	\$ 436,802	1.55%	07-03-03
Popular Bank of Puerto Rico	1110000119	4,500,000	1.55%	07-03-03
Popular Bank of Puerto Rico	1110000120	3,000,000	1.65%	09-01-03
Popular Bank of Puerto Rico	1110000121	5,000,000	1.65%	09-01-03
Popular Bank of Puerto Rico	1110000109	1,500,000	1.55%	07-02-03
Popular Bank of Puerto Rico	1110000125	4,000,000	1.65%	07-28-03
Popular Bank of Puerto Rico	1110000124	2,000,000	1.55%	08-24-03
Popular Bank of Puerto Rico	1110000117	<u>1,000,000</u>	1.55%	07-27-03
TOTAL		<u>\$21,436,802</u>		

The investments are distributed by the amounts of \$7,500,000 in the General Fund, \$1,000,000 in the Other Governmental Fund and \$12,936,802 in the Paseo Real Marina Fund.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 3 INTERFUND TRANSFER AND BALANCES

A. INTERFUND TRANSFERS

Transfers are indicative of funding for capital projects or debt service, and subsidies of various operations.

INTERFUND TRANSFERS WITHIN THE GOVERNMENTAL FUNDS

<u>SOURCES</u>	<u>TRANSFER TO</u>	<u>AMOUNT</u>	<u>PURPOSE</u>
General Fund	Debt Services Fund	\$ 304,202	Debt payments
General Fund	Other Fund	1,473,144	Specific project funding
Other Fund	Debt Services Fund	<u>1,705,000</u>	Debt payments
Total		<u>\$ 3,482,346</u>	

B. INTERFUND RECEIVABLE AND PAYABLE BALANCES

Interfund receivables and payables at June 30, 2003 are summarized as follows:

<u>INTERFUND RECEIVABLE</u>	<u>INTERFUND PAYABLE</u>	<u>AMOUNT</u>
General Fund	Special Revenue Fund	\$ 161,772
General Fund	CDBG	<u>11,658</u>
TOTAL		<u>\$ 173,430</u>

NOTE 4 DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2003, balance due to other governmental units of the General Fund for services rendered to the Municipality, consists of the following:

Water Company	\$ 61,781
Municipal Revenue Collection Center	18,686
PR Retirement System	<u>150</u>
Total Due to Government Units	<u>\$ 80,617</u>

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 5 CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2003 was as follows:

<u>DESCRIPTION</u>	<u>BALANCE JULY 1, 2002</u>	<u>ADDITIONS</u>	<u>RETIREMENTS</u>	<u>BALANCE JUNE 30, 2003</u>
Non-Depreciable Capital Assets:				
Land	\$18,626,446	\$ 270,620	\$ 857,342	\$18,039,724
Construction in Progress	<u>2,798,788</u>	<u>1,706,363</u>	<u>-</u>	<u>4,505,151</u>
Total Non-Depreciable Capital Assets ..	<u>21,425,234</u>	<u>1,976,983</u>	<u>857,342</u>	<u>22,544,875</u>
Depreciable Capital Assets:				
Buildings	53,948,567	1,010,703	-	54,959,270
Infrastructure	8,522,835	572,325	-	9,095,160
Motor Vehicles	6,637,888	223,376	-	6,861,264
Machinery and Equipment.....	<u>2,122,123</u>	<u>694,103</u>	<u>-</u>	<u>2,816,226</u>
Total Depreciable Capital Assets	<u>71,231,413</u>	<u>2,500,507</u>	<u>-</u>	<u>73,731,920</u>
Less Accumulated Depreciation:				
Buildings	(19,514,911)	(926,538)	-	(20,441,449)
Infrastructure	(606,594)	(145,227)	-	(751,821)
Motor Vehicles	(3,424,773)	(683,858)	-	(4,108,631)
Machinery and Equipment.....	<u>(1,329,133)</u>	<u>(285,812)</u>	<u>-</u>	<u>(1,614,945)</u>
Total Accumulated Depreciation.....	<u>(24,875,411)</u>	<u>(2,041,435)</u>	<u>-</u>	<u>(26,916,846)</u>
Total Depreciable Capital Assets (Net) .	<u>46,356,002</u>	<u>459,072</u>	<u>-</u>	<u>46,815,074</u>
CAPITAL ASSETS, NET	<u>\$67,781,236</u>	<u>\$ 2,436,055</u>	<u>\$ 857,342</u>	<u>\$69,359,949</u>

Depreciation expenses were charged to governmental functions/programs as follows:

	<u>AMOUNT</u>
Mayor and Municipal Legislature.....	\$ 95,506
General Government.....	159,590
Public Safety.....	82,408
Public Works.....	316,623
Health and Sanitation	197,111
Culture and Recreation	44,044
Human Services and Welfare.....	41,865
Urban Development	<u>1,104,288</u>
Total Depreciation Expenses.....	<u>\$2,041,435</u>

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 6 GENERAL LONG-TERM DEBTS

A. GENERAL OBLIGATIONS BONDS AND SPECIAL NOTES PAYABLE

The principal long-term obligations of the Municipality are general obligations bonds and special notes issued to finance the construction and improvements of public facilities and purchase of equipment. The Municipality's obligations long-term debt retirements are appropriated and paid from resources accumulated in the Debt Service Fund (See Note 9). The special obligations long-term notes retirements are paid through retention made by the Municipal Revenue Collection Center from monthly advance of annual property tax and subsidy send to the Municipality.

General obligations bonds and notes payable as of June 30, 2003, are comprised of the following individual issues:

<u>DESCRIPTION</u>	<u>AMOUNT</u>
General Obligations Bonds:	
\$590,000, Series 1999, payable in semiannual installments ranging from \$20,000 to \$70,000, excluding interests at 5.00%, through July 1, 2013	\$ 465,000
\$2,840,000, Series 1999, payable in semiannual installments ranging from \$105,000 to \$300,000, excluding interests at 5.30%, through July 1, 2013	2,215,000
\$5,065,000, Series 1999, payable in semiannual installments ranging from \$70,000 to \$425,000, excluding interests at 5.30%, through July 1, 2023	4,635,000
\$3,210,000, Series 1999, payable in semiannual installments ranging from \$45,000 to \$270,000, excluding interests at 2.80%, through July 1, 2023	2,935,000
\$1,700,000, Series 1999, payable in semiannual installments ranging from \$115,000 to \$230,000, excluding interests at 2.80%, through July 1, 2008	1,005,000
\$805,000, Series 1999, payable in semiannual installments ranging from \$5,000 to \$65,000, excluding interests at 2.70%, through July 1, 2023	740,000
\$3,520,000, Series 2000, payable in annual installments ranging from \$130,000 to \$370,000, excluding interests at 2.70%, through July 1, 2014	2,925,000

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 6 GENERAL LONG-TERM DEBTS, Continued

<u>DESCRIPTION</u>	<u>AMOUNT</u>
\$1,340,000, Series 2000, payable in annual installments ranging from \$15,000 to \$115,000, excluding interests at 2.70%, through July 1, 2024	1,265,000
\$975,000, Series 2000, payable in annual installments ranging from \$65,000 to \$135,000, excluding interests at 2.80%, through July 1, 2010	755,000
\$3,015,000, Series 2001, payable in annual installments ranging from \$65,000 to \$285,000, excluding interests at 2.80%, through July 1, 2020	\$ 2,805,000
\$1,010,000, Series 2001, payable in annual installments ranging from \$170,000 to \$240,000, excluding interests at 2.80%, through July 1, 2005	455,000
\$2,165,000, Series 2001, payable in annual installments ranging from \$25,000 to \$190,000, excluding interests at 2.80%, through July 1, 2025	2,075,000
\$565,000, Series 2003, payable in semiannual installments ranging from \$65,000 to \$100,000, excluding interests at 2.70%, through July 1, 2009	<u>500,000</u>
Total General Obligations Bonds	<u>22,775,000</u>
Special Obligations Notes:	
\$1,150,000, Series 1999, payable in semiannual installments ranging from \$130,000 to \$200,000, excluding interests at 5.30%, through July 1, 2005	390,000
\$12,995,000, Series 2002, payable in annual installments of \$650,000, excluding interests at 5.00%, through August 1, 2022 (HUD – Section 108 Loan)	12,995,000
\$4,795,000, Series 2003, payable in annual installments ranging from \$75,000 to \$370,000, excluding interests at 5.00%, through July 1, 2027	<u>4,720,000</u>
Total Special Obligations Bonds	<u>18,105,000</u>
Total General and Special Obligations Bonds	<u>\$40,880,000</u>

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 6 GENERAL LONG-TERM DEBTS, Continued

The Municipality's general obligations long-term note retirements are appropriated and paid from resources accumulated in the debt service fund (see Note 8). The special obligations long-term notes retirements are paid through retention made by the Municipal Revenue Collection Center from monthly advance of annual property tax and subsidy sent to the Municipality.

The annual requirements to amortize the general and special obligations outstanding as of June 30, 2003 are as follows:

Year Ending June 30,	Principal Payment	Interest Payment	Total Payment
2004	\$ 2,170,000	\$ 2,027,429	\$ 4,197,429
2005	2,295,000	1,979,449	4,274,449
2006	1,950,000	1,896,234	3,846,234
2007	2,040,000	1,760,603	3,800,603
2008	2,150,000	1,735,559	3,885,559
2009-2014	10,225,000	7,225,860	17,450,860
2015-2019	8,695,000	4,707,357	13,402,357
2020-2024	9,530,000	2,143,725	11,673,725
2025-2027	<u>1,825,000</u>	<u>245,720</u>	<u>2,070,720</u>
TOTAL	<u>\$40,880,000</u>	<u>\$23,721,936</u>	<u>\$64,601,936</u>

B. OTHER LONG-TERM DEBTS

DESCRIPTION	BALANCE JULY 1, 2002	NEW ISSUES	RETIREMENTS AND ADJUSTMENT	BALANCE JUNE 30, 2003
Property Taxes – MRCC	\$ 126,158	\$ -	\$ -	\$ 126,158
Unemployment	136,771	-	136,771	-
Landfill Closure and Post-closure costs .	-	800,000	-	800,000
Claims and Judgments	1,000,000	-	500,000	500,000
Compensated Absences	<u>2,813,131</u>	<u>51,466</u>	<u>-</u>	<u>2,864,597</u>
TOTAL	<u>\$ 4,076,060</u>	<u>\$ 851,466</u>	<u>\$ 636,771</u>	<u>\$ 4,290,755</u>

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 6 GENERAL LONG-TERM DEBTS, Continued

C. CHANGES IN GENERAL LONG-TERM DEBTS

The following is a summary of changes in long-term debts for the year ended June 30, 2003:

DESCRIPTION	BALANCE JULY 1, 2002	NEW ISSUES	RETIREMENTS AND ADJUSTMENT	BALANCE JUNE 30, 2003	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
General.....	\$23,370,000	\$ 565,000	\$ 1,160,000	\$22,775,000	\$ 1,475,000	\$21,300,000
Special.....	2,410,000	17,790,000	2,095,000	18,105,000	790,000	17,315,000
Others Debts ...	<u>4,076,060</u>	<u>851,466</u>	<u>636,771</u>	<u>4,290,755</u>	<u>3,270,436</u>	<u>1,020,319</u>
TOTAL	<u>\$29,856,060</u>	<u>\$19,206,466</u>	<u>\$ 3,891,771</u>	<u>\$45,170,755</u>	<u>\$ 5,535,436</u>	<u>\$39,635,319</u>

NOTE 7 DEBT RETIREMENT

Revenues of the debt service fund consists of the ad-valorem property taxes which are recognized as revenue when collected from taxpayers and reported by the Municipal Revenue Collection Center of the Commonwealth of Puerto Rico to the Municipality (See Note 9).

These property taxes are accumulated by the Municipal Revenue Collection Center in costs of the general obligations bonds issued by the Municipality (See Note 7). Payments are made to the Government Development Bank of the Commonwealth of Puerto Rico from such accumulated funds by the Municipal Revenue Collection Center of Puerto Rico.

NOTE 8 PROPERTY TAXES

The Municipal Revenue Collection Center of the Commonwealth of Puerto Rico is responsible for the assessment of all real and personal property located within the Municipality and for the levy, administration and collection of the corresponding tax contribution.

The property tax contribution is levied each year over the appraised value of the property at the beginning of the calendar year. The real property assessment is based on the current value existing in the year 1957 and the personal property at the current value at the date of the assessment.

The tax rate per annum is 8.53% for real property and 6.53% for personal property of which 1.03% of both belong to the Commonwealth of Puerto Rico and 7.50% and 5.50%, respectively, belongs to the Municipality. From the portion belonging to the Municipality, 6.00% and 4.00%, respectively, represents the Municipality's basic tax rate that is appropriated for general purposes and therefore accounted for through the general fund.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 8 PROPERTY TAXES, Continued

The remaining portion belonging to the Municipality of 1.50% represents the ad-valorem property taxes withheld by the Municipal Revenue Collection Center of the Commonwealth of Puerto Rico and restricted for debt service, which is accounted for through the debt service fund (See Note 8). The Municipality has reached the maximum statutory tax rate limit for the basic tax while there is no limitation for the ad-valorem tax rate.

The Commonwealth of Puerto Rico grants complete real property tax exoneration on the first \$15,000 has assessed valuation on residential units occupied by their owners. However, the Municipality receives the full amount levied, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. The Municipal Revenue Collection Center, instead of the property taxpayer, becomes the source of payment in these cases.

The Municipality grants a complete exemption from personal property taxes up to an assessment value of \$50,000, to retailers with an annual net sales volume of less than \$150,000. The Municipal Revenue Collection Center advances to the Municipality, on monthly payments, 100% of the contribution assessed over property for each fiscal year. In accordance to Law, these advances will be contributions by the Municipal Revenue Collection Center from taxpayers. The Municipal Revenue Collection Center periodically informs to the Municipality the amounts collected from taxpayers and applied to outstanding advances.

The Municipality records as revenue in the general fund the property tax contribution when received from monthly advances from Municipal Revenue Collection Center.

Due to the fact that collections of property tax are applied to the advances of property tax paid by the Municipality Revenue Collection Center, the amortization of the advance at end of year was not available due to that is in process of verification by external auditors.

NOTE 9 VOLUME OF BUSINESS TAX

The volume of business tax is levied each year based on the prior year's gross revenues for all commercial and industrial organizations doing business in the Municipality and which are not totally or partially exempt from this tax under the Industrial Incentives Laws of the Commonwealth of Puerto Rico. All taxpayers are required to file their declarations by April 23 of each year. The tax rates are as follows:

- a. 1.50% for financial institutions and savings and loan associations.
- b. 0.40% for all other organizations.

Taxes are payable in two equal semi-annual installments on July 1 and January 1 following the date of levy. If they are paid with declaration, the taxpayer is granted a 5% of discount. Collections of taxes during current fiscal year, applicable to the next fiscal year, are recorded as deferred revenues in the General Fund.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 10 INTERGOVERNMENTAL REVENUES

Intergovernmental revenues consist primarily of funds received from the Commonwealth of Puerto Rico, "in lieu of tax" payments from the quasi-public corporation, Puerto Rico Electric Power Authority, and federal financial assistance received from federal government.

Grants and subsidies received from the Commonwealth of Puerto Rico and federal agencies include, among others, a general subsidy for urban development and capital improvements. Intergovernmental revenues are accounted for through the General Fund except for those directly related to urban development and capital improvements, which are accounted for through the Special Revenue and the Capital Project Funds. Federal Financial Assistance is recorded in the Special Revenue Fund.

NOTE 11 EMPLOYEE'S RETIREMENT PLAN

The Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) is the administrator of a cost-sharing multiple-employer retirement system established by the Commonwealth of Puerto Rico. The ERS was created under the Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentalities and of certain municipalities and components units not covered by their own retirement systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Head of Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of the Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees. ERS provides retirement, death and disability benefits. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

The Municipality adopted the requirements of GASBS No. 25 for all the career employees that are covered under the Commonwealth of Puerto Rico Employee's Retirement System, a multiple-employer public employee retirement system, established by State Laws.

Under the plan, the employees and employer portions are contributed, for which, the employee amount is withheld from salaries. Covered employees are required by Commonwealth statute to contribute 5.775% for the first \$550 of monthly salary plus 8.275% for the excess of this amount, or on the alternative, 8.275% of all salary. The Municipality contributes to the system 9.275% of the participating employee's salaries.

Law Number 305 of September 24, 1999, amends the Act Number 447 that establish a savings program. All employees active in the system as of December 31, 1999 may elect to transfer from defined contribution programs to the new savings program (a defined contribution plan). Employees in the savings program may now contribute from a minimum of 8.275% up to a maximum of 10% of their monthly salary, and will be invested in an account which will either: (a) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (b) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (c) earn a combination of both alternatives.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 11 EMPLOYEE'S RETIREMENT PLAN, Continued

If at time of retirement accumulated benefits amount to \$10,000 or less may elect to receive a lump sum distribution up to the accumulated benefits. Under the new program the retirement age is reduced from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

The pension benefit for participants who retire with less than 30 years of service is computed at the rate of 1½% of their average compensation of each year of credit service for the remaining years. The System also provides for death and disability benefits and the assets of the System pertaining to the participant employees.

A variety of significant actuarial assumptions are used to determine the standard measure of the pension benefit obligation and these assumptions are summarized below:

- a. The present value of the future pension payments was computed by using a discount of 9%.
- b. Future pension payments reflect an assumption of a 6% salary increase.

All employees that do not elect to transfer for the new program, and who at the time of employment are 55 years old or less are eligible to participate in the System. Pension benefits for participants with 30 years of service are as follows:

<u>YEARS OF SERVICE</u>	<u>PARTICIPANT'S AGE</u>	<u>PENSION BENEFITS</u>
30 or more	55 or less	65% of the average of the three years of highest salary during the employee's service period.
30 or more	58 or more	75% of the average of the three years of highest salary during the employee's service period.
30 or more	65 or more	75% of the average of the three years of highest salary during the employee's service period (employees started working after April 1, 1990).

The amount of the total pension benefit obligation is based on a standardized measurement established by GASBS No. 27, *Financial Reporting for Defined Benefit Pension Plans and Notes Disclosure for Defined Contributions Plans*. The standardized measurement is the actuarial present value of estimated defined pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee services performed to date. The measure is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among other public retirement systems. The measure is independent of the actuarial funding method used to determine contributions to the plan.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 11 EMPLOYEE'S RETIREMENT PLAN, Continued

The membership of retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits, but not yet receiving benefits, and active employees and the distribution of active employees between vested and non-vested is not readily available.

Contributions in 2003 and prior years were made based on percentages established by the law. Such percentage has not been based on actuarial studies, as required by accounting principles generally accepted in the United States of America. An actuarial compilation of the annual contribution applicable to the Municipality has not been prepared. Accordingly, the accounts by which the actual contributions differ from the required actuarial contributions are not known.

The total pension expenditures recorded in the category of administration for the fiscal year ended June 30, 2003 was approximately \$715,978. All employees who at the time of employment are 55 years old or less are eligible to participate in the System. No benefit is payable if the participant receives a refund of his accumulated contributions.

The historical trend information regarding the accumulation of assets and pension benefit obligation in the ERS is not available. For the ten-year trend information, refer to the separately issued financial statements of the ERS as of and for the fiscal year ended June 30, 2003. The P.R. Retirement Plan Administration provides additional information of the ERS. They issue a public available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Commonwealth of Puerto Rico. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, PR 00940.

NOTE 12 CONTINGENCIES

A. CLAIMS AND JUDGMENTS

The Municipality is, at present, a defendant in a number of legal matters that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities. The legal counsel of the Municipality has advised that at this stage in the proceedings of lawsuits he recommend a reserve of \$500,000 which is included in the statement of net assets.

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in discovery stage. Certain of these claims are covered by insurance. Legal counsel with the information currently available can not determine the final outcome of these claims. Accordingly, the financial statements do not include adjustment, if any, that could result from the resolution of this legal proceeding. However, it has been the Municipality's experience that such actions are settled for amounts substantially less than the claimed amounts.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 12 CONTINGENCIES, Continued

B. FEDERAL GRANTS

In the normal course of operations, the Municipality receives grants from various Federal and State agencies. The grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

The Municipality is, at present, a defendant in a number of legal matters that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities. The legal counsels of the Municipality have advised that at this stage in the proceedings of lawsuits he cannot offer an opinion as to the probable outcome.

NOTE 13 ESTIMATED MUNICIPAL SOLID WASTE LANDFILL CLOSING COSTS

According to the Environmental Protection Agency's (EPA) regulations, the Municipality must follow certain closure functions and postclosure monitoring and maintenance procedures. In addition, the Municipality has not adopted the **GASB Number 18** in order to comply with these regulations.

As of June 30, 2002, the Municipality proceeds with the rehabilitation of an inactive landfill. According with the study performed the landfill qualify to received additional waste material during a maximum of estimated useful file of 2 years. The total estimated closing and postclosing costs in accordance with the study is \$1,250,000 that will be recognized in the financial statements as require by this accounting policy. Of this amount a total of \$800,000 (64% of the estimated life) was recognized as expense during fiscal year 2002-2003 with a reimbursement to the Municipality of \$243,367 for the proceeds of the collections for the material deposited in the landfill. The amount due to the private company should be paid when the closing is performing during the following year.

NOTE 14 ACCOUNTING CHANGES, CHANGES IN REPORTING ENTITY AND RESTATEMENTS

During fiscal year 2002-2003, the Municipality implemented several new accounting standards and an interpretation issued by GASB.

GASBS No. 34 as amended by GASBS No. 37 establishes new financial reporting standards for state and local governments. This statement's requirements represent a significant change in the financial reporting model used by state and local governments, including statement formats and changes in fund types and elimination of account groups. In addition to fund financial statements, governments are required to report government-wide financial statements, prepared using the accrual basis of accounting and the economic resources measurement focus. As a result, fund reclassifications and adjustments to the fund equities reported in the prior financial statement balances were required.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO THE BASIC FINANCIAL STATEMENTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 14 ACCOUNTING CHANGES, CHANGES IN REPORTING ENTITY AND RESTATEMENTS, Continued

GASBS No. 38 requires certain note disclosures when GASBS No. 34 is implemented. The provisions of these new standards have been incorporated into the basic financial statements and notes. GASB Interpretation No. 6 clarifies the application of existing standards for distinguishing the respective portions of certain types of liabilities that should be reported as (1) governmental fund liabilities and (2) general long-term liabilities of the government. The provisions of this interpretation have been incorporated into the basic financial statements and notes.

These new accounting standards caused most of the accounting changes, changes in reporting entity, and restatements described on the ensuing discussions below. Changes and restatements for reasons other than the adoption of the above pronouncements are also explained below.

The following schedule reconciles the June 30, 2002 Fund Balances, as previously reported to Beginning Fund Balances, as restated, July 1, 2002.

FUND BALANCE RESTATED

	<u>GENERAL</u>	<u>HEAD START</u>	<u>DEBT SERVICE</u>	<u>CDBG</u>	<u>OTHERS GOVERNMENTAL FUNDS</u>
Fund Balance (Deficit)/Net Assets, as Reported, June 30, 2002	\$1,278,222	\$ -	\$5,079,895	\$ -	\$3,091,838
Adjustment to Cash Accounts.....	(1,094,435)	-	-	-	2,589,689
Adjustment to Expenditures for Change in Accounting Principles.....	-	-	(2,576,938)	-	-
Adjustment to revenues in accordance with GAAP.....	-	<u>897,747</u>	-	<u>2,926</u>	<u>22,036</u>
Beginning Fund Balance, as Restated, July 1, 2002.....	<u>\$ 183,787</u>	<u>\$ 897,747</u>	<u>\$2,502,957</u>	<u>\$ 2,926</u>	<u>\$5,703,563</u>

NOTE 15 FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENT

The Governmental Accounting Standards Board (GASB) issued GASBS No. 39, *Determining Whether Certain Organizations are Component Units*, which is effective for fiscal year beginning after June 15, 2003. The Municipality has not adopted the requirement of this statement.

END OF NOTES

MUNICIPALITY OF AGUADILLA, PUERTO RICO

REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2003

MUNICIPALITY OF AGUADILLA, PUERTO RICO
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

	BUDGET AMOUNTS		ACTUAL AMOUNTS (BUDGETARY BASIS) (SEE NOTE A)	VARIANCE WITH FINAL BUDGET POSITIVE (NEGATIVE)
	ORIGINAL	FINAL		
BUDGETARY FUND BALANCE, JULY 1, 2002	\$ 183,787	\$ 183,787	\$ 183,787	\$ -
Resources (Inflows):				
Property Taxes	8,133,925	8,133,925	8,724,617	590,692
Volume of Business Taxes	8,170,000	8,670,000	9,275,555	605,555
Intergovernmental Revenues	5,157,080	5,157,080	5,015,103	(141,977)
License and Permits	509,839	289,311	851,182	561,871
Rent	829,040	549,568	259,120	(290,448)
Miscellaneous	830,800	3,020,550	3,013,057	(7,491)
Total Resources (Inflows).....	23,630,684	25,820,434	27,138,634	1,318,202
Amounts Available for Appropriation.....	23,814,471	26,004,221	27,322,421	1,318,200
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	2,694,834	3,102,391	2,873,229	229,162
General Government	10,771,850	10,796,098	10,027,742	768,356
Public Safety	1,606,903	1,566,770	1,520,950	45,820
Public Works	1,540,436	1,678,958	1,618,285	60,673
Health and Sanitation	2,767,561	2,646,964	2,598,018	48,946
Culture and Recreation	777,651	976,882	956,044	20,838
Urban Development	35,000	457,337	441,620	15,717
Human Services and Welfare	2,806,554	2,866,662	2,807,483	59,179
Capital Outlays	111,445	285,083	278,537	6,546
Transfer to Other Funds	518,450	1,443,289	1,304,202	139,087
Total Charges to Appropriations.....	23,630,684	25,820,434	24,426,110	1,394,324
BUDGETARY FUND BALANCE, JUNE 30, 2003.....	\$ 183,787	\$ 183,787	\$ 2,896,311	\$ 2,712,524

See accompanying Notes to Required Supplementary Information.

MUNICIPALITY OF AGUADILLA, PUERTO RICO
NOTE TO BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE A Explanation of Differences between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures

	<u>GENERAL FUND</u>
Sources/Inflows of Resources:	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 39)	\$ 27,322,421
Difference – Budget to GAAP:	
The Fund Balance at the Beginning of Year is a budgetary resource but is not a Current-Year Revenue for financial reporting purposes.....	(183,787)
Prior-Year Revenue is inflows of budgetary resources but are not <i>revenues</i> for financial reporting purposes.....	(18,686)
The proceeds from the sale of assets are budgetary resources but are regarded as a <i>special item</i> , rather than revenue, for financial reporting purposes.....	<u>(2,189,750)</u>
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 12).....	<u>\$ 24,930,198</u>
Uses/Outflows of Resources:	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 39)	\$ 24,426,110
Difference – Budget to GAAP:	
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes.....	(386,639)
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes.....	<u>(1,304,202)</u>
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 12).....	<u>\$ 22,735,269</u>

NOTE B Explanation of Differences Between Budgetary Fund Balance and GAAP Fund Balance

Budgetary Fund Balance, June 30, 2003 (See Page 39).....	\$ 2,896,311
Timing Differences:	
Net Change in Encumbrances	(866,421)
Non-budgetary Items.....	<u>(491,830)</u>
Unrestricted Fund Balance, June 30, 2003 (See Page 12).....	<u>\$ 1,538,151</u>

END OF THIS SECTION

MUNICIPALITY OF AGUADILLA, PUERTO RICO

SINGLE AUDIT SECTION

YEAR ENDED JUNE 30, 2003

MUNICIPALITY OF AGUADILLA, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

Federal Grantor / Pass Through Grantor / Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. Department of Agriculture:			
Pass-Through Administration of Families and Children:			
Child and Adult Care Food Program (USDA)	10.558	CCC-07-AG	\$ 431,337
Pass-Trough Office of the Governor – Elderly Office			
Child and Adult Care Food Program (USDA)	10.558	N/A/V	<u>36,029</u>
Total U.S. Department of Agriculture			<u>467,366</u>
U.S. Department of Housing and Urban Development:			
Direct Programs:			
Community Development Block Grants/ Entitlement Grants (CDBG)	14.218		3,516,755
Urban Development Action Grant	14.221		293,200
Emergency Shelter Grant Program	14.231		58,657
Home Investment Partnership Program (HOME)	14.239		418,089
Community Development Block Grant Section 108 Loan Guarantees (Note 8)	14.248		12,995,000
Section 8 Rental Housing Choice Vouchers	14.871		<u>1,058,205</u>
Total U.S. Department of Housing and Urban Development			<u>18,339,906</u>
U.S. Department of Justice:			
Direct Programs:			
Weed and Seed	16.595		91,360
Pass Through Puerto Rico Department of Justice:			
Local Law Enforcement Block Grant	16.592	99-LB-VX-0726	<u>101,270</u>
			<u>192,630</u>
Subtotal Expenditures of Federal Awards (Balance Carry Forward)			<u>18,999,902</u>

Continue

MUNICIPALITY OF AGUADILLA, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS, Continue
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

Federal Grantor / Pass Through Grantor / Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
Subtotal of Expenditures of Federal Awards (Balance Brought Forward)			<u>\$18,999,902</u>
U.S. Department of Health and Human Services:			
Pass-Through Office of the Governor – Elderly Office:			
Special Program for Aging, Title III, Part B	93.044	N/AV	140,467
Special Program for Aging, Title III, Part C	93.045	N/AV	160,227
Pass-Through Administration of Families and Children:			
Head Start Program	93.600	02-CH-0483-35	
	93.600	02-CH-0483-36	5,617,329
Community Service Block Grant (CSBG)	93.569		<u>25,000</u>
Total U.S. Department of Health and Human Services			<u>5,943,023</u>
Corporation for National and Community Service (CNS):			
Vista Project Support	94.013	N/AV	<u>13,908</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$24,956,833</u>

The accompanying Notes to Schedule of Expenditures of Federal Awards are an integral of this Schedule.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 1 GENERAL

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activities of the **Municipality of Aguadilla, Puerto Rico**. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits 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 basic financial statements. The Municipality reporting entity is defined in Note (1) (A) to the basic financial statements. All federal financial awards received directly from federal agency as well as federal financial awards passed through other government agencies are included on the Schedule.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. The accompanying Schedule of Expenditures of Federal Awards is prepared from Municipality's accounting records and is not intended to present financial position or the results of operations.
- B. The Municipality in accordance with the terms records the financial transactions and conditions of the grants, which are consistent with accounting principles generally accepted in the United States of America.
- C. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable or when actually paid, whichever occurs first.

NOTE 3 FEDERAL CFDA NUMBER

The CFDA numbers included in this Schedule are determined based on the program name, review of grant contract information and the Office of Management and Budget's Catalogue of Federal Domestic Assistance.

NOTE 4 PASS THROUGH GRANTOR'S NUMBER

State or local government redistribution of federal awards to the Municipality, treated as if they were received directly from the federal government. OMB Circular A-133 requires the schedule to include the name of the pass through entity and identifying number assigned by the pass through entity for federal awards received as a subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

MUNICIPALITY OF AGUADILLA, PUERTO RICO

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS, Continued

FOR THE FISCAL YEAR ENDED JUNE 30, 2003

NOTE 5 RELATIONSHIP TO GENERAL-PURPOSE COMBINED FINANCIAL STATEMENTS

Federal financial assistance expenditures are reported in the Municipality's Combined Statement of Revenues, Expenditures and Change in Fund Balance-All Governmental Fund Types as follows:

<u>Description</u>	<u>Head Start Fund</u>	<u>CDBG Fund</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Federal Programs Expenditures	\$5,617,329	\$3,516,755	\$2,827,749	\$11,961,833
State and Municipal Expenditures	-	-	4,198,064	4,198,064
Total Expenditures	<u>\$5,617,329</u>	<u>\$3,516,755</u>	<u>\$7,025,813</u>	<u>\$16,159,897</u>

NOTE 6 SUBRECIPIENTS

Of the federal expenditures presented in the Schedule, the Municipality, provided federal awards to subrecipients as follows:

<u>Program Title</u>	<u>Federal CFDA Number</u>	<u>Amount Provided To Subrecipients</u>
Community Development Block Grant-Entitlement Grants (CDBG)	14.218	\$102,345
Emergency Shelter Grant Program (ESG)	14.231	58,201
HOME Investment Partnership Program (HOME)	14.239	<u>103,615</u>
Total		<u>\$264,161</u>

NOTE 7 MAJOR PROGRAMS

Major programs are identified in the Summary of Auditor's Results Section of the Schedule of Findings and Questioned Costs.

NOTE 8 COMMUNITY DEVELOPMENT BLOCK GRANT SECTION 108 LOAN GUARANTEES

Represent a non cash program that involve a loan guarantee from the Secretary of Housing and Urban Development pursuant to Section 108 of Title I of Housing and Community Act of 1974. Conforming Section 205(b) of OMB Circular A-133 the award expended is the outstanding balance of loan received.

END OF NOTES



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Juan E. Román Toro, MBA, CPA
José D. Román Toro, CPA

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

Honorable Mayor and Members of the
Municipal Assembly
Municipality of Aguadilla, Puerto Rico

We have audited the basic financial statements of **Municipality of Aguadilla, Puerto Rico**, as of and for the year ended June 30, 2003, and have issued our report thereon dated December 12, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

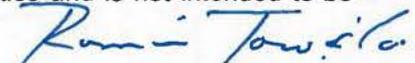
Compliance

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

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Municipality of Aguadilla's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a 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 in amounts that would be material in relation to the basic 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. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the management, office of the Commissioner of Municipal Affairs, and 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.


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Yauco, Puerto Rico
December 12, 2003

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José D. Román Toro, CPA

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

Honorable Mayor and Members of the
Municipal Assembly
Municipality of Aguadilla, Puerto Rico

Compliance

We have audited the compliance of **Municipality of Aguadilla, 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, 2003. Municipality of Aguadilla's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Municipality of Aguadilla's management. Our responsibility is to express an opinion on Municipality of Aguadilla's compliance based on our audit.

We conducted our 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 States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance 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 Aguadilla's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Municipality of Aguadilla's compliance with those requirements.

In our opinion, Municipality of Aguadilla, Puerto Rico complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2003.

Internal Control Over Compliance

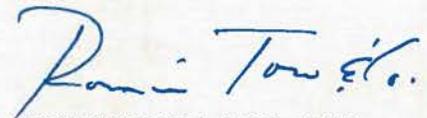
The management of Municipality of Aguadilla, Puerto Rico, is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Municipality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

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

(CONTINUED)

Our 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 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 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. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the management, office of the Commissioner of Municipal Affairs, and 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.



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Yauco, Puerto Rico
December 12, 2003

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**MUNICIPALITY OF AGUADILLA, PUERTO RICO
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 FOR THE YEAR ENDED JUNE 30, 2003**

SECTION I – SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditor's report issued: Unqualified Opinion Qualified Opinion
 Adverse Opinion Disclaimer Opinion

Internal control over financial reporting:

- Reportable condition(s) identified? Yes None reported
- Material weakness (es) identified? Yes No
- Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

- Reportable condition(s) identified? Yes None reported
- Material weakness (es) identified? Yes No

Type of auditor's report issued on compliance for Major Programs:

Unqualified Opinion Qualified Opinion
 Adverse Opinion Disclaimer Opinion

Any audit finding disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133?

Yes No

Identification of Major Programs:

CFDA Number	Name of Federal Program or Cluster
10.558	Child and Adult Care Food Program
14.239	Home Investment Partnership Program
14.248	Community Development Block Grant Section 108 Loan Guarantees
16.592	Local Law Enforcement Block Grant
93.600	Head Start Program

Dollar threshold used to distinguish between Type A and Type B Programs:

\$358,855

Auditee qualified as low-risk auditee?

Yes No

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (Continued)
FOR THE YEAR ENDED JUNE 30, 2003**

SECTION II – FINANCIAL STATEMENT FINDINGS

None

**SECTION III – FINANCIAL AWARD FINDINGS AND
QUESTIONED COSTS**

None

**MUNICIPALITY OF AGUADILLA, PUERTO RICO
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2003**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Cost	Comments
(1) Audit Findings that have been fully corrected:					
2002	02-111-01	Municipality did not obtain the required licenses for various Head Start Centers	93.600	None	The management obtained the required licenses from the state agencies. No similar findings were noted in 2003 audit.
(2) Audit Findings not corrected or partially corrected:					
NONE					
(3) Corrective action taken is significantly different from corrective action previously reported:					
NONE					
(4) Audit findings is no longer valid:					
NONE					
END OF SCHEDULE					

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