

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES  
ÁREA DE ASESORAMIENTO, REGLAMENTACIÓN E INTERVENCIÓN FISCAL  
ÁREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE AGUAS BUENAS  
AUDITORÍA 2009-2010  
30 DE JUNIO DE 2010**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SINGLE AUDIT REPORTING PACKAGE  
FOR THE YEAR ENDED JUNE 30, 2010**

OFICINA DEL COMISIONADO  
DE ASUNTOS MUNICIPALES  
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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SINGLE AUDIT REPORTING PACKAGE  
FOR THE YEAR ENDED JUNE 30, 2010**

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**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED JUNE 30, 2010**

*Carlos R. Diaz Negrón*

Certified Public Accountant

MEMBER:

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

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## INDEPENDENT AUDITOR'S REPORT

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

We have audited the financial statements of the governmental activities, each major funds, and the aggregate remaining fund information of the **Municipality of Aguas Buenas, Puerto Rico** as of and for the year ended June 30, 2010 which collectively comprise the basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the business-type activities. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Espiritu Santo Project, is based solely on the report of the other auditors.

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 the Governmental Audit Standards, issued by the Comptroller General of the United State. 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, based on our audit and the report of other auditors, 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 Aguas Buenas, Puerto Rico** as of June 30, 2010, and the respective changes in financial position for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.



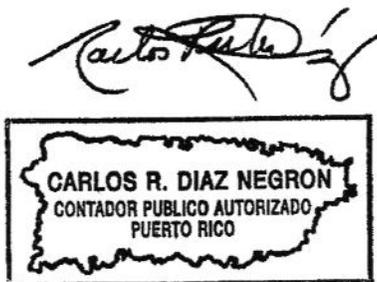
**INDEPENDENT AUDITOR'S REPORT (CONTINUED):**

In accordance with Governmental Auditing Standards, we have also issued our report dated November 22, 2010, on our consideration of the Municipality of Aguas Buenas, Puerto Rico' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Governmental Auditing Standards and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 12 and 42 through 45 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

November 22, 2010  
Aguas Buenas, Puerto Rico

License No. 1339  
Expire December 1, 2013



The stamp No. **2564395** of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**YEAR ENDED JUNE 30, 2010**

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This discussion and analysis of the Municipality of Aguas Buenas, Puerto Rico (Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2010. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2009. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

1. a broader basis in focusing important issues;
2. acknowledgement of an overview of the Municipality's financial activities;
3. provide for an evaluation of its financial condition as of the end of the indicated fiscal year, compared with prior year results;
4. identification of uses of funds in the financing of the Municipality's variety of activities and;
5. assess management's ability to handle budgetary functions.

**FINANCIAL HIGHLIGHTS**

The following comments about the financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2010 deserve special mention:

1. Total assets of the Municipality amounted to \$28,094,475 which represents an increase of 3% compared to prior fiscal year.
2. At the end of fiscal year 2010, total liabilities amounted to \$10,536,755. Out of said amount, \$8,307,019 corresponded to long-term liabilities of which \$4,575,000 represented the outstanding balance of bonds and notes issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.
3. Total net assets of the Municipality amounted to \$17,557,720 which represents an increase of 7% compared to prior fiscal year, as restated.
4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$15,665,005 derived from the following sources: \$387,229 charges for services; \$2,085,592 from operating grants and contributions; \$2,510,360 from capital grants and contributions obtained from other sources, and \$10,681,823 from general revenues available.
5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$14,650,619.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

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**FINANCIAL HIGHLIGHTS (CONTINUED)**

6. As reflected in the Statement of Activities, the current fiscal year operations contributed to an increase in the Net Assets figure by \$1,014,386.
7. As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$2,900,654.
8. As the end of the current fiscal year, the Municipality's general fund balance amounted to \$45,789, compared to a fund balance of \$163,890 in the prior fiscal year.
9. The actual General Fund budgetary activities resulted in an unfavorable balance of \$152,644.

**FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION**

The approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2010. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

Under the aforementioned approach, assets and liabilities are recognized using the accrual basis of accounting which is similar to the method used by most private enterprises. This means that current year's revenues and expenses are accounted for regardless of when cash is received or paid.

**FINANCIAL STATEMENTS COMPONENTS**

The basic financial statements consist of the government wide financial statements, the major funds financial statements and the notes to the financial statements which provide details, disclosure and description of the most important items included in said statements.

The Statement of Net Assets reflects information of the Municipality as a whole of a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year. Such financial level is measured as the difference between total assets and liabilities, with the difference between both items reported as net assets. It is important to note that although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations. The higher the increments achieved in net revenues, the higher the capacity to increase the net assets figure either thru additional borrowings or thru internally generated funds. This in turn will benefit the welfare of the Municipality of Aguas Buenas, Puerto Rico constituents.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

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**FINANCIAL STATEMENTS COMPONENTS (CONTINUED)**

The Statement of Activities is focused on both gross and net cost of the various activities of the Municipality. It presents information which shows the changes in the Municipality's net assets at the most recent fiscal year. Based on the use of the accrual basis of accounting, changes are reported as soon as the underlying event occurs, regardless of the timing of the related cash flows. Under said approach, revenues and expenses are reported in the Statement of Activities based on the theory that it will result in cash flows to be realized in future periods.

A brief review of the Statements of Activities of the Municipality at June 30, 2010, shows total expenses incurred to afford the cost of all functions and programs amounted to \$14,650,619. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$4,983,181 was derived from the following sources: \$387,229 charges for services; \$2,085,592 from operating grants and contributions; and \$2,510,360 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$10,681,283. When such figure is added to the \$4,983,181 previously mentioned, total revenues available for the financing of activities amounted to \$15,665,005. There was an excess of revenues over expenses in the amount of \$1,014,386 which contributed with an increase to the figure of net assets attained at the end of the fiscal year.

The Fund Financial Statement is another important component of the Municipality's financial statements. A fund is a grouping of related accounts that are used to maintain accountability and controls over economic resources of the Municipality that have been segregated for specific activities. The Municipal fund type of accounting is used to demonstrate compliance with related legal requirements. Information offered thru this Statement is limited to the Municipality most significant funds and is particularly related to the local government only, instead of the government as a whole. Government funds are used to account for essentially the same functions as those reported as governmental activities. The funds are reported using an accounting method known as modified accrual accounting which measures cash and all other financial assets that can be readily converted into cash.

The fund statement approach gives the user a short term view of the Municipality's government operations and the basic services it provides. Since the focus of government funds is narrower than that of the financial statements as a whole, it also helps the user with comparable information presented in the governmental activities report. By doing so, readers of the basic financial statements may understand better the long-term effect of the Municipality's short-term financial decisions.

**INFRASTRUCTURE ASSETS**

Historically, a significant group of infrastructure assets (such as roads, bridges, traffic signals, underground pipes not associated with utilities, etc.) have not been recognized nor depreciated in the accounting records of the Municipality. GASB 34 requires that such type of assets be inventoried, valued and reported under the governmental column of the Government-Wide Statement.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

**INFRASTRUCTURE ASSETS (CONTINUED)**

According to the requirements of GASB 34, the government must elect to either (a) depreciate the aforementioned assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery to near perpetuity. If the government develops the asset management system, (the modified approach) which periodically (at least every three years), by category, measures and demonstrate its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. In this particular respect, the Municipality has elected the use of recognizing depreciation under the useful life method and it contemplates to continue this treatment on said basis.

**FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE**

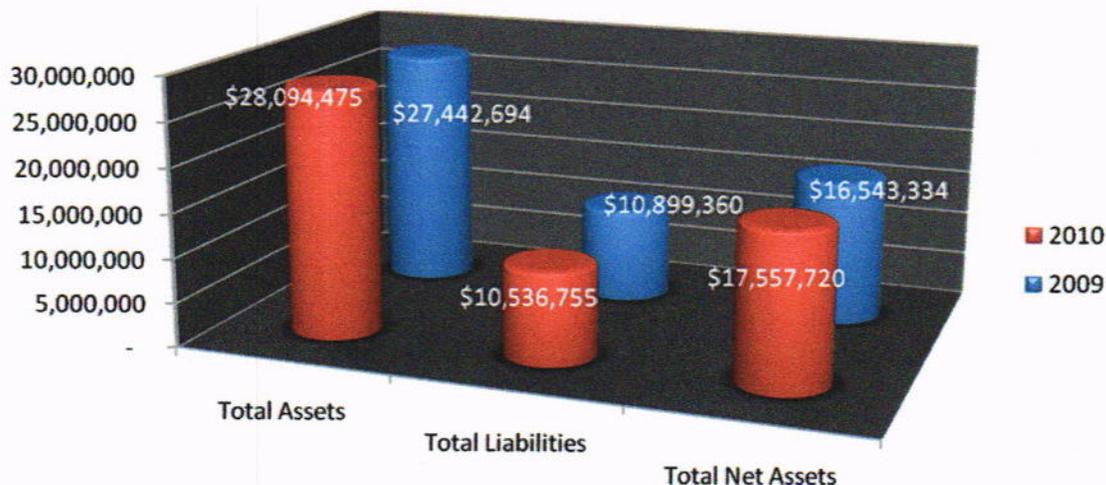
**Net Assets**

The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Aguas Buenas, Puerto Rico, primary government assets exceeded total liabilities by \$17,557,720 at the end of 2010, compared to \$16,543,334, as restated, at the end of the previous year, as showed in the following condensed Statement of Net Assets of the Primary Government.

<u>Condensed Statement of Net Assets</u>	<u>2010</u>	<u>2009</u>	<u>Change</u>	<u>%</u>
Current and other assets	6,645,566	7,540,884	(895,318)	-12%
Capital Assets	<u>21,448,909</u>	<u>19,901,810</u>	<u>1,547,099</u>	8%
Total Assets	<u>28,094,475</u>	<u>27,442,694</u>	<u>651,781</u>	2%
Current and other liabilities	2,229,736	2,627,468	(397,732)	-15%
Long-term liabilities	<u>8,307,019</u>	<u>8,271,892</u>	<u>35,127</u>	(2)%
Total liabilities	<u>10,536,755</u>	<u>10,899,360</u>	<u>(362,605)</u>	-3%
Invested in capital assets, net of related debt	17,204,257	15,419,693	1,784,564	12%
Restricted	2,675,651	3,397,521	(721,870)	(5)%
Unrestricted deficit	<u>(2,322,188)</u>	<u>(2,273,880)</u>	<u>(48,308)</u>	2%
Total net assets	<u>\$ 17,557,720</u>	<u>\$ 16,543,334</u>	<u>\$ 1,014,386</u>	6%

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

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Approximately 28 percent of the Municipality's total revenue came from taxes, while 67 percent resulted from grants and contributions, including federal aid. Charges for Services provide 3 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for public work and sanitation (34%), general government (24 %), and educational, culture and recreational (13%). As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

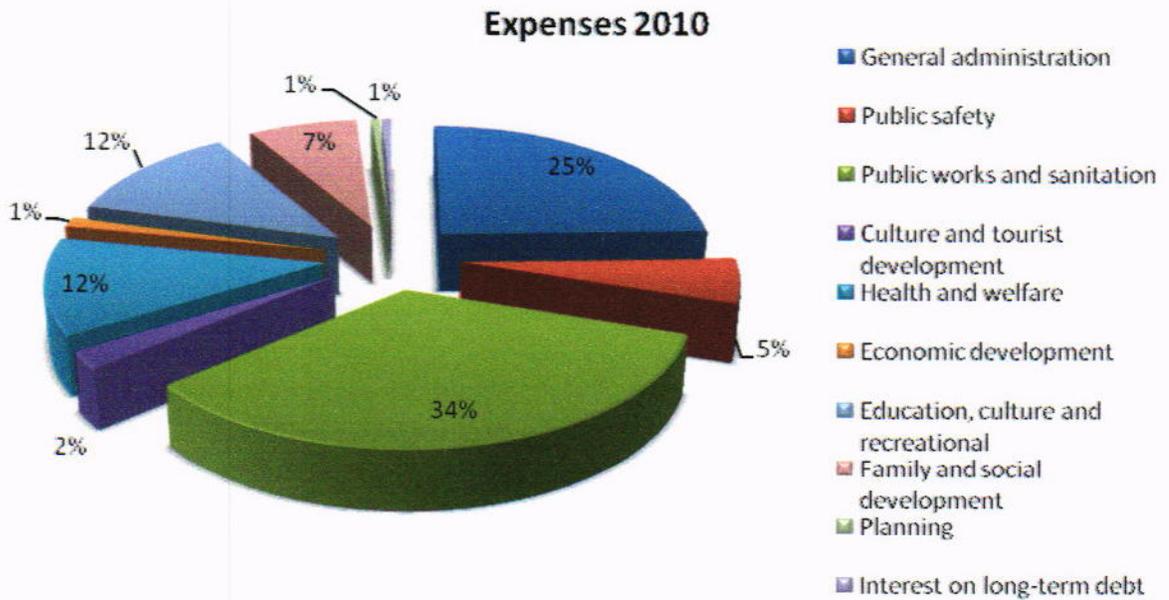
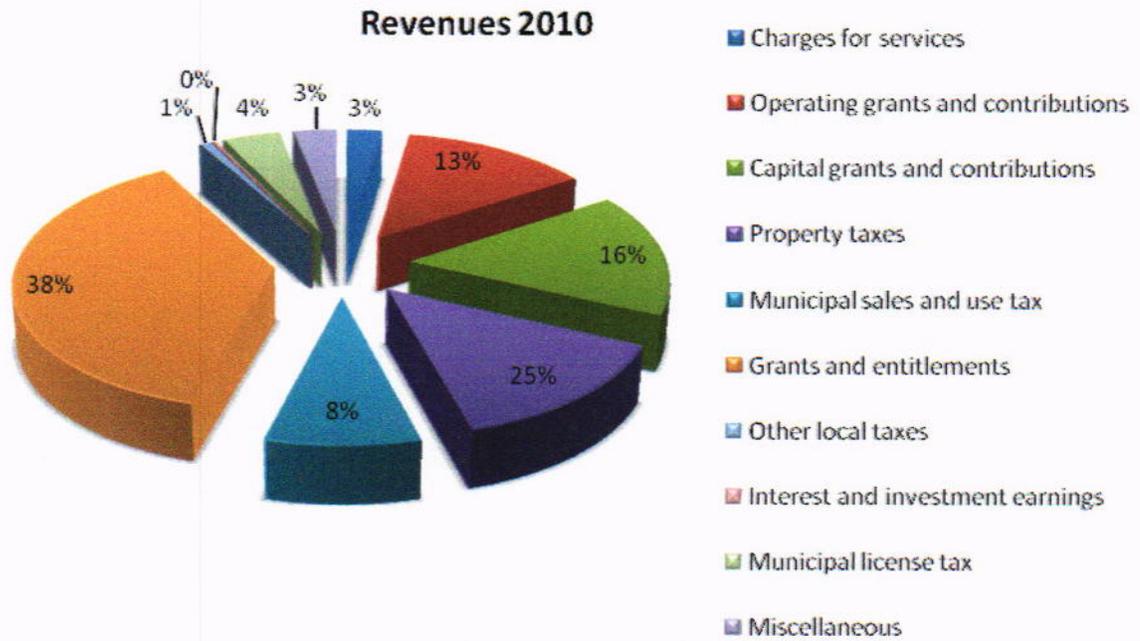
**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

**FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)**

<b>Condensed Statement of Activities</b>	<b>2010</b>	<b>2009</b>	<b>Change</b>	<b>%</b>
<b>Program revenues:</b>				
Charges for services	\$ 387,229	\$ 372,305	\$ 14,924	4%
Operating grants and contributions	2,085,592	3,208,961	(1,123,369)	(35%)
Capital grants and contributions	2,510,360	5,373,537	(2,863,177)	(53%)
<b>General revenues:</b>				
Property taxes	2,183,284	1,587,939	595,345	37%
Municipal license tax	646,481	656,446	(9,965)	(2%)
Municipal sales and use tax	1,311,377	1,141,105	170,272	15%
Grants and entitlements	5,885,052	6,373,687	(488,635)	(8%)
Other local taxes	123,270	312,445	(189,175)	(61%)
Interest and investment earnings	43,726	61,094	(17,368)	(28%)
Other	488,634	873,856	(385,222)	(44%)
<b>Total revenues</b>	<b>15,665,005</b>	<b>19,961,375</b>	<b>(4,296,370)</b>	<b>(22%)</b>
<b>Expenses:</b>				
General administration	3,518,109	3,677,229	(159,120)	(4%)
Public safety	779,839	693,592	86,247	12%
Public works and sanitation	4,891,331	10,432,200	(5,540,869)	(53%)
Health and welfare	1,690,119	2,109,703	(419,584)	(20%)
Culture and tourist development	311,533		311,533	100%
Economic development	167,643		167,643	100%
Family and social development	1,060,442		1,060,442	100%
Planning	86,060		86,060	100%
Public relations and citizen affairs		567,218	(567,218)	(100%)
Education, culture and recreational	1,755,202	1,182,477	572,725	48%
Housing	300,683	291,814	8,869	3%
Interest	89,658	279,827	(190,169)	(68%)
<b>Total expenses</b>	<b>14,650,619</b>	<b>19,234,060</b>	<b>(4,583,441)</b>	<b>(24%)</b>
Change in net assets	1,014,386	727,315	287,071	39%
Net assets	16,543,334	15,816,019	727,315	5%
Net assets, end of year	\$ 17,557,720	\$ 16,543,334	\$ 1,014,386	6%

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)  
YEAR ENDED JUNE 30, 2010**

**FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)**



**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

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**FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS**

**Governmental Funds**

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$2,900,654, a decrease of \$636,101 in comparison with the prior year.

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2010, the general fund has an undesignated fund balance of \$45,789.

**GENERAL FUND BUDGETARY HIGHLIGHTS**

Over the course of the year, the Municipality Legislative Body revised the Municipality's budget in order to include increases in revenues that were identified during the course of the fiscal year based on current developments that positively affected the Municipality's finances. Increases in budgeted expenditures were also made since the law mandates a balanced budget.

The actual General Fund budgetary activities resulted in an unfavorable balance of \$152,644 caused mainly due to unexpected variances in revenue and expenditures.

**CAPITAL ASSETS AND DEBT ADMINISTRATION**

**Capital Assets**

The Municipality's investment in capital assets as of June 30, 2010, amounts to \$35,846,514, with an accumulated depreciation of \$14,397,605 (including depreciation charges for the year totaled \$1,021,299), leaving a net book value of \$21,448,909. This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure, furnishing, computers and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2010, the Municipality has \$1,437,377 of unexpended proceeds mainly from bonds and notes issuances that are committed to future construction activities.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

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**CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)**

**Debt Administration**

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged.

The applicable law also requires that, in order for a Municipality to be able to issue additional general obligation bonds and notes, such Municipality must have sufficient "payment capacity". Act No. 64 provides that a Municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, will be sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues.

Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available but the revenue also is very predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2009-2010.

The American Recovery and Reinvestment Act of 2009, abbreviated ARRA, is an economic stimulus package endorsed by the President of the United States of America and approved by Congress. Its immediate goals include the creation of new jobs as well as save existing ones, preserve the economic activity, invest in long-term economic growth, and promote a high level of accountability and transparency in government spending.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)**  
**YEAR ENDED JUNE 30, 2010**

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**ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES (CONTINUED)**

Puerto Rico is part of the American territories that will benefit from the stimulus package of ARRA, and will receive approximately \$5,600 million in grants and is eligible to obtain additional funding through other competitive federal programs.

As part of this plan, the Municipality of Aguas Buenas, Puerto Rico will benefit from federal grants to improve its services to its constituents and from the economic activity generated within its territory due to projects funded by ARRA.

**FINAL COMMENTS**

The Municipality is an autonomous governmental entity whose powers and authority vested on its Executive and Legislative Branches are specifically established in the Municipal Autonomous Act approved in August 1991. By virtue of such powers, it provides a wide range of services to its constituents which includes, among others, public works, education, public safety, public housing, health, community development, recreation, waste disposal, welfare and others. The Municipality's principal sources of revenues are derived from property taxes, municipal license taxes, subsidies from the Commonwealth of Puerto Rico's General Fund and contributions from the Traditional and Electronic Lottery sponsored by said Government.

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. It further contemplates to maintain or improve its current levels of Net Assets as indicative of a strong financial position which has been identified as one of the main short and long-term objectives of the Municipality.

**FINANCIAL CONTACT**

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer.

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**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**STATEMENT OF NET ASSETS**  
**AS OF JUNE 30, 2010**

ASSETS	PRIMARY GOVERNMENT		
	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS – TYPE ACTIVITIES</u>	<u>TOTAL</u>
Cash and cash equivalents	\$ 2,028,490	\$125,635	\$ 2,154,125
Cash with fiscal agent	1,437,377		1,437,377
Investment in certificates of deposit	500,000		500,000
Account receivable:			
Other agencies	939,110		939,110
Property tax	1,296,719		1,296,719
Sale tax	106,436		106,436
Municipal tax	2,682		2,682
Other assets		39,521	169,596
Restricted cash		169,596	169,596
Capital assets, net	<u>20,942,574</u>	<u>506,335</u>	<u>21,448,909</u>
<b>Total Assets</b>	<b><u>\$ 27,253,388</u></b>	<b><u>\$841,087</u></b>	<b><u>\$28,094,475</u></b>
<b>LIABILITIES AND NET ASSETS</b>			
<b>Liabilities:</b>			
Accounts payable and accrued expenses	\$ 1,323,759	\$ 17,695	\$ 1,341,454
Deferred revenue	804,846		804,846
Due to other agencies	83,436		83,436
Long-term debt:			
Due within one year	1,103,041	44,869	1,147,910
Due in more than one year	<u>6,679,914</u>	<u>479,195</u>	<u>7,159,109</u>
<b>Total liabilities</b>	<b><u>9,994,996</u></b>	<b><u>541,759</u></b>	<b><u>10,536,755</u></b>
<b>Net Assets:</b>			
Invested in capital assets, net of related debt	17,204,257		17,204,257
Restricted for:			
Debt service	899,692		899,692
Replacements and others		169,596	169,596
Capital project and others	1,606,363		1,606,363
Unrestricted	<u>(2,451,920)</u>	<u>129,732</u>	<u>(2,322,188)</u>
<b>Total Net Assets</b>	<b><u>\$ 17,258,392</u></b>	<b><u>\$299,328</u></b>	<b><u>\$17,557,720</u></b>

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**STATEMENT OF ACTIVITIES**  
**FOR THE YEAR ENDED JUNE 30, 2010**

<u><b>FUNCTIONS AND PROGRAMS</b></u>	<u><b>EXPENSES</b></u>	<u><b>PROGRAM REVENUE</b></u>			<u><b>NET (EXPENSE)/ REVENUE</b></u>
		<u><b>CHARGE FOR SERVICES</b></u>	<u><b>OPERATING GRANTS AND CONTRIBUTIONS</b></u>	<u><b>CAPITAL GRANTS AND CONTRIBUTIONS</b></u>	
Governmental activities:					
General administration	\$ (3,518,109)	\$ 1,856	\$ 176,681		\$ (3,339,572)
Public safety	(779,839)		64,823		(715,016)
Education, culture and recreational	(1,755,202)	60,437	527,255		(1,167,510)
Public works and sanitation	(4,891,331)			\$2,510,360	(2,380,971)
Health and welfare	(1,690,119)		1,316,833		(373,286)
Culture and tourist development	(311,533)				(311,533)
Economic development	(167,643)				(167,643)
Family and social development	(1,060,442)				(1,060,442)
Planning	(86,060)				(86,060)
Interest	<u>(89,658)</u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>(89,658)</u>
Total governmental activities	(14,349,936)	62,293	2,085,592	2,510,360	(9,691,691)
Business type-activities:					
Housing	<u>(300,683)</u>	<u>324,936</u>	<u>          </u>	<u>          </u>	<u>24,253</u>
Total	<u><u>\$(14,650,619)</u></u>	<u><u>\$387,229</u></u>	<u><u>\$2,085,592</u></u>	<u><u>\$2,510,360</u></u>	<u><u>\$ (9,667,438)</u></u>

(Continue)

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
STATEMENT OF ACTIVITIES (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS-TYPE ACTIVITIES</u>	<u>TOTAL</u>
Net (expense)/revenue	<u>\$ (9,691,691)</u>	<u>\$24,253</u>	<u>\$(9,667,438)</u>
General revenue:			
Taxes:			
Property taxes	2,183,284		2,183,284
Municipal tax	646,481		646,481
Sale tax	1,311,377		1,311,377
Construction excise tax	123,270		123,270
Grants and entitlements	5,885,052		5,885,052
Rent	107,022		107,022
Interest	43,185	541	43,726
Other	<u>381,612</u>	<u>          </u>	<u>381,612</u>
Total general revenues	<u>10,681,283</u>	<u>541</u>	<u>10,681,824</u>
Changes in net assets	989,592	24,794	1,014,386
Net assets at beginning	<u>16,268,800</u>	<u>\$274,534</u>	<u>16,543,334</u>
Net assets at end	<u>\$ 17,258,392</u>	<u>\$299,328</u>	<u>\$ 17,557,720</u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS**

**BALANCE SHEET  
GOVERNMENTAL FUNDS  
AS OF JUNE 30, 2010**

	<b>GENERAL FUND</b>	<b>DEBT SERVICE</b>	<b>OTHER GOVERNMENTAL FUNDS</b>	<b>TOTAL GOVERNMENTAL FUNDS</b>
<b>Cash:</b>				
Cash in bank	\$ 355,385		\$1,673,105	\$2,028,490
Cash with fiscal agent	12,306	\$1,265,345	159,726	1,437,377
Investment in saving certificates	500,000			500,000
<b>Receivables:</b>				
Property taxes	993,093	303,626		1,296,719
Sale tax		35,355	71,081	106,436
Due for others governmental agencies	50,046		889,064	939,110
Due from other funds	254,690			254,690
Other	<u>2,682</u>	_____	_____	<u>2,682</u>
<b>Total assets</b>	<b><u>\$2,168,202</u></b>	<b><u>\$1,604,326</u></b>	<b><u>\$2,792,976</u></b>	<b><u>\$6,565,504</u></b>
<b>Liabilities:</b>				
Accounts payable and accrued expenses	\$ 550,612		\$ 719,517	\$1,270,129
Deferred revenues	1,488,365	\$ 293,096	275,134	2,056,595
Due to other fund			254,690	254,690
Due to other agencies	<u>83,436</u>	_____	_____	<u>83,436</u>
<b>Total liabilities</b>	<b><u>2,122,413</u></b>	<b><u>293,096</u></b>	<b><u>1,249,341</u></b>	<b><u>3,664,850</u></b>
<b>Fund balance</b>				
Unreserved	45,789	1,311,230		1,357,019
Unreserved reported in non major:				
Capital project			995,926	985,926
Special funds	_____	_____	<u>557,709</u>	<u>557,709</u>
<b>Total fund balance</b>	<b><u>45,789</u></b>	<b><u>1,311,230</u></b>	<b><u>1,543,635</u></b>	<b><u>2,900,654</u></b>
<b>Total liabilities and fund balance</b>	<b><u>\$2,168,202</u></b>	<b><u>\$1,604,326</u></b>	<b><u>\$2,792,976</u></b>	<b><u>\$6,565,504</u></b>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
RECONCILIATION OF THE GOVERNMENTAL FUNDS  
BALANCE SHEET TO THE STATEMENT OF NET ASSETS  
AS OF JUNE 30, 2010**

<b>Fund balances in governmental funds</b>	<b>\$ 2,900,654</b>
 <i>Amounts reported for governmental activities in the Statement of Net Assets are different because:</i>	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds	20,942,574
Deferred property tax revenue in governmental funds financial statements whereas recorded as revenue in the governmental activities	1,251,749
Long-term liabilities and accrual expenses are not due and payable in the current period and therefore are not reported in the governmental funds:	
Bonds and notes payable	(4,575,000)
Compensated absences	(1,664,159)
Estimated liability for landfill post-closure costs	(1,360,000)
Accrued interest	(53,630)
Other long term debt	(183,796)
<b><i>Net assets of governmental activities</i></b>	<b><u>\$17,258,392</u></b>

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**STATEMENT OF REVENUES, EXPENDITURES**  
**AND CHANGES IN FUND BALANCE-GOVERNMENTAL FUNDS**  
**FOR THE YEAR ENDED JUNE 30, 2010**

	<u>GENERAL FUND</u>	<u>DEBT SERVICE FUNDS</u>	<u>OTHER GOVERNMENTAL FUNDS</u>	<u>TOTAL GOVERNMENTAL FUNDS</u>
<b>Revenues:</b>				
Taxes:				
Property taxes	\$1,645,656	\$ 507,248		\$ 2,152,904
Municipal taxes	646,481			646,481
Sale tax		411,695	\$ 899,682	1,311,377
Excise taxes	123,270			123,270
Interest	42,800	385		43,185
Rental income	107,022			107,022
Grants and entitlements	5,822,760		4,658,244	10,481,004
Other	<u>443,905</u>			<u>443,905</u>
<b>Total Revenues</b>	<u>8,831,894</u>	<u>919,328</u>	<u>5,557,926</u>	<u>15,309,148</u>
<b>Expenditures:</b>				
General administration	2,956,798		349,171	3,305,969
Public safety	624,753		82,641	707,394
Education and recreational	768,864		727,687	1,496,551
Public works and sanitation	2,777,820		3,850,412	6,628,732
Health and welfare	332,016		1,297,116	1,629,132
Culture and tourist development	274,876		26,386	301,262
Economic development	167,643			167,643
Family and social development	844,286		181,195	1,025,481
Planning	17,526		68,534	86,060
Debt service:				
Principal		429,000		429,000
Interest		<u>168,525</u>		<u>168,525</u>
<b>Total expenditures</b>	<u>8,764,582</u>	<u>597,525</u>	<u>6,583,142</u>	<u>15,945,249</u>
<b>Excess (deficiency) of revenue over expenditures</b>	<u>67,312</u>	<u>321,803</u>	<u>(1,025,216)</u>	<u>(639,101)</u>
<b>Other financing sources (uses):</b>				
Operating transfer in	385	185,798		186,183
Operating transfer out	(185,798)	(385)		(186,183)
Proceed from loan				
<b>Total other financing sources</b>	<u>(185,413)</u>	<u>185,413</u>		
<b>Excess of revenues and other financing source over (under) expenditures and other financing sources</b>	(118,101)	507,216	(1,025,216)	(636,101)
<b>Fund balance at beginning of year</b>	<u>163,890</u>	<u>804,014</u>	<u>2,568,851</u>	<u>3,536,755</u>
<b>Fund balance at end of year</b>	<u>\$ 45,789</u>	<u>\$1,311,230</u>	<u>\$ 1,543,635</u>	<u>\$ 2,900,654</u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES  
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL  
FUNDS TO THE STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2010**

**Net change in fund balances – total governmental funds** \$(636,101)

*Amounts reported for Governmental Activities in the Statement of Activities are different because:*

Governmental funds report capital outlays as expenditures. However, in the statement of activities and changes in net assets, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount of capital assets recorded in the current period. 2,555,986

Governmental funds report principal payments on long-term debts as expenditures, whereas the principal payments reduce the long-term debt in the statement of net assets. 429,000

Change in accrued expenses which does not require the use of current financial resources:

Accrued interest	78,867
Compensating absences	(514,585)
Other long-term debts	9,028
Deferred propriety tax	30,380

Depreciation expense on capital assets is reported in the statement of activities, but it does not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditure in governmental funds. (962,983)

***Changes in Net Assets of Governmental Activities*** \$(989,592)

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**STATEMENT OF FINANCIAL POSITION – PROPRIETARY FUND**  
**JUNE 30, 2010**

**ASSETS**

	<b>BUSINESS TYPE ACTIVITIES ESPIRITU SANTO PROJECT</b>
<b>Current Assets:</b>	
Cash	\$125,635
Property and Equipment	506,335
Restricted deposits	169,596
Other Assets	<u>39,521</u>
	<u>\$841,087</u>

**LIABILITIES AND NET ASSETS**

<b>Liabilities:</b>	
Current liabilities:	
Current maturities of mortgage note	\$ 44,869
Accounts payable and accrued expenses	<u>17,695</u>
	62,564
Long term-debt, net of current maturities	<u>479,195</u>
	541,759
<b>Net assets</b>	<u>299,328</u>
<b>Total liabilities and net assets</b>	<u>\$841,087</u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
STATEMENT OF ACTIVITIES - PROPRIETARY FUND  
YEAR ENDED JUNE 30, 2010**

	<b>BUSINESS TYPE ACTIVITIES ESPIRITU SANTO PROJECT</b>
<b>Revenues:</b>	
Rent	\$324,936
Financial	<u>541</u>
<b>Total revenues</b>	<u><b>325,477</b></u>
<b>Expenses:</b>	
Administrative	90,523
Utilities	5,666
Operating Maintenance	74,371
Taxes and insurance	34,080
Depreciation	58,316
Interest	<u>37,727</u>
<b>Total Expenses</b>	<u><b>300,683</b></u>
<b>Change in net assets</b>	24,794
Project net assets, beginning of year	<u>274,534</u>
<b>Project net assets, and year</b>	<u><b>\$299,328</b></u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS  
FOR THE YEAR ENDED JUNE 30, 2010**

	<b>BUSINESS TYPE ACTIVITIES ESPIRITU SANTO PROJECT</b>
<b>Cash flow from operating activities:</b>	
Cash received from rentals	\$338,866
Interest received	<u>541</u>
	<u>339,407</u>
Administrative	34,786
Utilities	13,278
Salaries and wages	105,350
Operating and maintenance	31,985
Property and liability insurance	5,757
Interest on mortgage	37,371
Management fees	<u>23,400</u>
	<u>251,927</u>
 <b>Net cash provided by operating activities</b>	 <u>87,480</u>
<b>Cash flow from investing activities:</b>	
Purchase of equipment	(12,412)
Deductions from reserve for replacements and interest	<u>28,052</u>
<b>Net cash used by investing activities</b>	15,640
<b>Cash flows from financing activities:</b>	
Mortgage principal payments	<u>(41,430)</u>
<b>Net cash used by financing activities</b>	<u>(41,430)</u>
<b>Net increase in cash</b>	61,690
<b>Cash at beginning of the year</b>	<u>63,945</u>
<b>Cash at ending of the year</b>	<u>\$125,635</u>

(Continue)

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

**Reconciliation of change in net assets to net cash provided by operating activities:**

	<b>BUSINESS TYPE ACTIVITIES ESPIRITU SANTO PROJECT</b>
<b>Cash flow from operating activities:</b>	
<b>Change in net assets</b>	<u>\$ 24,794</u>
<b>Adjustments to reconcile change in net assets to net cash provided by operating activities:</b>	
Depreciation	58,316
Increase (decrease) in:	
Account receivable (net)	13,564
Accounts payable	(6,954)
Accrued vacations and bonus	(2,606)
Interest on mortgage	<u>366</u>
<b>Total adjustments</b>	<u>62,686</u>
<b>Net cash provided by operating activities</b>	<u>\$ 87,480</u>

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2010**

**1. ORGANIZATION**

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

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

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

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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

**Reporting entity**

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

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

**Government wide and fund financial statements**

Basic financial statements include both governments-wide and fund financial statements.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Government-wide statements

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

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

Program-specific capital and operating grant and contributions consist of transactions that are either mandatory or voluntary nonexchange transactions with other governments, organizations, or individuals that restrict the resources for use in a particular program. Capital grants and contributions consist of capital assets or resources that are restricted for capital purposes – to purchase, construct or renovate capital assets associated with a specific program. Operating grants and contributions consist of resources that are required to be used to finance the costs of operating a specific program or can be used either for operating or capital purposes of a specific program. Restricted capital and operating grants and contributions are program revenues because they are specifically attributable to a program are reducing the net expense of that program to the Municipality. They are reported net of estimated uncollectible amounts.

Fund financial statements

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

The Municipality reports the following major governmental funds:

A) General Fund

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

B) Debit service fund

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

**Measurement focus, basis of accounting and financial statement presentation**

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

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

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

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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

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

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

Proprietary fund financial statements include a statement of net assets, a statement of revenues, expenses and changes in fund nets, and statements of cash flows for the proprietary fund which include a low income housing project know as Espiritu Santo Project.

The Municipality has elected to not apply all statements and interpretation issued by FASB after November 30, 1989.

Proprietary funds are accounted for using the "economic resources" measurement focus and the accrual basis of accounting. Accordingly, all assets and liabilities (whether current or noncurrent) are include on the statement of net assets. The statement of revenues, expenses and change in fund net assets present increases (revenues) and decrease (expenses) in total net assets. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned while expenses are recognized in the period in which the liability is incurred.

Operating revenues in the proprietary fund are those revenues that are generated from the primary operating of the fund. All other revenues are reported as non-operating revenues. Operating expenses are those expenses that are essential to the primary operations of the fund. All other expenses are reported as non-operating expenses.

**Cash, cash equivalents, cash with fiscal agent and investment**

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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

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

**Interfund receivables and payables**

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

**Capital assets**

Capital assets, which include property, plant, equipment, and infrastructure (which is normally immovable and of value only to the Municipality, such as roads, bridges, streets sidewalks, and drainage system), are reported in the government-wide financial statements.

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

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

Infrastructure	50 years
Building	40 years
Improvement to land	25 years
Vehicles	7 years
Machinery and equipment	10 years
Computer and printer	3 years
Furniture	15 years

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Reservation of fund balance**

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

A) Debt/ service

Represents net assets available to finance future debt service payments.

B) State and federal programs

Represent the reservations of amounts available for specific use under state and federal grant programs.

**Risk financing**

The Municipality carries insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center (the "CRIM") for the year ended June 30, 2010 amounted to approximately \$171,770. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$156,913 for workers compensation insurance covering all municipal employees.

**Compensated absences**

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

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

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Post employment benefits**

Pursuant various Acts, the Municipality is required to cover annually the 3% increase (cost of living allowance) in the retirement plan of it's retirees employees. Substantially all of the employees may become eligible for these benefits of they reach normal retirement to while working for the Municipality. For the fiscal year ended June 30, 2010, post employment benefits retirees amounted to \$50,000. These benefits are recorded as expenditures when paid in the general fund.

**Use of estimates**

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

**3. PROPERTY TAX**

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

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

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

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**3. PROPERTY TAX (CONTINUED)**

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

The annual rate for fiscal year 2010 is 8.78% for real property and 6.78% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 6.0% and 4.0%, respectively, represent the Municipality's basic property tax rate, which is appropriated for general purposes and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.75% represents the special ad valorem tax restricted for debt service and accounted for in the debt service fund. . The Commonwealth contributes an annual tax rate of 0.2% of the property tax collected and the remaining rate is imposed to the taxpayer.

On January 26, 2000, Public Law, as amended, was enacted which authorized the CRIM to obtain a loan up to \$200 million, and for a term not exceeding 30 years, to allow for the financing of the debt that the municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year 2000-2001. The amount that the municipalities will collect from the additional property taxes resulting from the increase in the subsidy from the central government to the municipalities was assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law 238, enacted on August 15, 1999. As of June 30, 2010, the amount due to CRIM amounting to \$86,817 is presented as other long-term debt (see Note 9).

Total property tax receivable, net of an allowance for uncollectible accounts of \$6,561,429, amounted to \$1,296,719 at June 30, 2010. The composition of property taxes receivable and the related deferred revenues is as follows at June 30, 2010:

	<u>General Fund</u>	<u>Debt service Fund</u>	<u>Total</u>
Gross property taxes receivable	\$6,018,167	\$1,839,981	\$7,858,148
Less allowance for uncollectible accounts	<u>5,025,074</u>	<u>1,536,355</u>	<u>6,561,429</u>
Net property taxes receivable	<u>\$ 993,093</u>	<u>\$ 303,626</u>	<u>\$1,296,719</u>
 Deferred (unavailable property) tax revenues in GFFS	 <u>\$ 958,653</u>	 <u>\$ 293,096</u>	 <u>\$1,251,749</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**4. VOLUME OF BUSINESS TAX**

The municipal license tax is levied annually based on the volume of business of certain businesses and industrial organizations that operate in the Municipality. The tax rates are 1.50% for financing institutions and .50% for the other business institutions. The taxpayers must file a return not later than April 15 of every year and the tax is payable in two installments, due in July 1 and January 1 of the following fiscal year. The amount levied could be paid with a five percent (5%) discount if payment is made on or before the filing date. The Municipality levied and collected during the year ended June 30, 2010, \$529,712 corresponding to the following fiscal year volume of business tax. This amount was recorded as deferred revenue, and is presented as a liability in the accompanying financial statements.

**5. SALE TAX**

Pursuant to an amendment to Puerto Rico Internal Revenue Code, Act 117 of July 4, 2006, the Municipal Legislature approved the Ordinance 6, Series 2006-2007 to established a city tax contribution, effective November 1, 2006, to 1.5% over all transactions of sales of goods and services made on Aguas Buenas's boundaries. According to the Ordinance, these new resources will be principally used in the following activities: repairs and improvements of Municipal roads, infrastructure and sport facilities, construction of curbs and sidewalk, purchases of heavy equipment.

Municipality of Aguas Buenas, Puerto Rico contracted a service organization to manage the imposition and collection of the sales tax.

Pursuant to the provisions of the Law Number 80 of July, 29, 2007 and effective August 1, 2007, the citizenship contribution was uniformly established in 1.5%, for all the municipalities in Puerto Rico, of which 1% will be collected by the municipalities and the remaining .5% will be collected by the Treasury Department of the Commonwealth of Puerto Rico. A portion of those funds will be deposited in the Puerto Rico Governmental Development Bank, as a redemption fund, for financing capital projects to the municipalities.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**6. GRANTS AND ENTITLEMENTS REVENUE**

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

**7. DEFERRED REVENUE**

Deferred revenue consists of the followings:

Municipal license tax collected in the fiscal year 2008-2009 corresponding to the following fiscal year	\$ 529,712
Portion of grants received for which qualifying expenditures have not been incurred.	275,134
Property tax deferred for governmental fund financial statement and recurred as income in the governmental wide financial statements.	<u>1,251,749</u>
	<u>\$2,056,595</u>

**8. RESTRICTED DEPOSIT**

Restricted cash in the business-type activities consists of:

Tenant security deposits	\$ 8,661
Reserve for replacement	<u>160,935</u>
	<u>\$169,596</u>

Under the regulatory agreement, Project is required to set aside amounts for the replacement of property and other Project expenditures approved by HUD. HUD – Restricted Deposits are held in separate accounts and generally are not available for operating purposes.

Tenant's Security Deposit and its accumulated interest are held in a separate bank savings account in the name of the Project, in compliance with USDA-RD and HUD requirements. Any amounts not returned to the tenant due to lease violations are transferred to the Project's general operating account.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**9. CAPITAL ASSETS**

Capital asset activity for the year ended June 30, 2010 was as follows:

Primary Government	Balance June 30, 2009	Increases	Decreases	Balance June 30, 2010
<b>Governmental activities:</b>				
Capital assets, not being depreciated:				
Land	\$ 1,971,577	\$ 145,800		\$ 2,117,377
Construction in progress	<u>1,971,577</u>	<u>1,454,914</u>		<u>1,454,914</u>
		<u>1,600,714</u>		<u>3,572,291</u>
Capital assets being depreciated:				
Infrastructure	1,631,315	267,150		1,898,465
Buildings, park and courts	22,879,102	17,290		22,896,392
Machinery and equipment	2,386,481	636,481		3,022,962
Automobiles	<u>2,263,293</u>	<u>34,351</u>		<u>2,297,644</u>
Total capital assets being depreciated	<u>29,160,191</u>	<u>955,272</u>		<u>30,115,463</u>
Less accumulated depreciation for:				
Infrastructure	133,531	35,758		169,289
Buildings, parks and courts	8,522,681	572,230		9,094,911
Machinery and equipment	1,341,490	201,499		1,542,989
Vehicles	<u>1,784,495</u>	<u>153,496</u>		<u>1,937,991</u>
Total	<u>11,782,197</u>	<u>962,983</u>		<u>12,745,180</u>
Total depreciable capital assets, net	<u>17,377,994</u>	<u>(7,711)</u>		<u>17,370,283</u>
<b>Governmental activities capital assets net</b>	<u>19,349,571</u>	<u>1,593,003</u>		<u>20,942,574</u>
<b>Business-type activities:</b>				
Capital assets net being depreciated:				
Land	<u>50,700</u>			<u>50,700</u>
Capital assets being depreciated:				
Building and improvements	1,959,236	32,386		1,959,262
Equipment	<u>136,412</u>	<u>12,386</u>	<u>(32,360)</u>	<u>148,798</u>
	2,095,648	44,772	<u>(32,360)</u>	2,108,060
Less accumulated depreciation:				
Building and improvements and equipment	<u>1,594,109</u>	<u>58,316</u>		<u>1,652,425</u>
Total depreciable capital assets, net	<u>501,539</u>	<u>(13,544)</u>	<u>(32,360)</u>	<u>455,635</u>
<b>Business activities capital assets, net</b>	<u>552,239</u>	<u>(13,544)</u>	<u>(32,360)</u>	<u>506,335</u>
	<u>\$19,901,810</u>	<u>\$1,579,459</u>	<u>\$(32,360)</u>	<u>\$21,448,909</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**9. CAPITAL ASSETS (CONTINUED)**

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

	<b>Governmental Activities</b>	<b>Business-Type Activities</b>
General administration	\$108,462	
Public safety	48,328	
Public works	593,115	
Education, culture and recreation	207,631	
Health, sanitation and welfare	5,447	
Housing	<u>          </u>	<u>\$58,316</u>
Total depreciation expense	<u>\$962,983</u>	<u>\$58,316</u>

**10. LONG-TERM DEBTS**

Long-term liability activity for the year ended June 30, 2010 was as follows:

<b>Primary Government Governmental activities:</b>	<b>Beginning Balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>Ending Balance</b>	<b>Due within one year</b>
Bonds and notes	\$5,004,000		\$429,000	\$4,575,000	\$ 297,000
Other long-term debt:					
Compensated absences	1,149,574	\$514,585		1,664,159	800,000
Amount due to CRIM	192,824		9,028	183,796	6,041
Landfill	<u>1,360,000</u>	<u>          </u>	<u>          </u>	<u>1,360,000</u>	<u>          </u>
Total	7,706,398	514,585	438,028	7,782,955	1,103,041
<b>Business-type activities:</b>					
Mortgage payable	<u>565,494</u>	<u>          </u>	<u>41,430</u>	<u>524,064</u>	<u>44,869</u>
Total	<u>\$8,271,892</u>	<u>\$514,585</u>	<u>\$479,458</u>	<u>\$8,307,019</u>	<u>\$1,147,910</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**10. LONG-TERM DEBTS (CONTINUED)**

**Governmental activities:**

Bonds and notes:

\$920,000 Public Improvement Serial Bonds of 1995 payable in annual installments of \$35,000 to \$85,000 through July 1, 2020 plus interest at 6.12%.	\$ 25,000
\$600,000 Public Improvement Serial Bonds of 1993 payable in annual installments ranging from \$35,000 to \$48,000 through January 1, 2015, plus interest at 6%.	210,000
\$400,000 Public Improvement Bonds, Serial of 1997 Payable in annual installments ranging from \$24,000 to \$34,000 through January1, 2016, plus interest at 5.62%.	175,000
\$2,285,000 General Obligation Bonds, Serial 1998-99 payable in annual installments ranging from \$45,000 to \$175,000, through July 1, 2030, plus interest at 6.5%.	2,125,000
\$255,000 General Obligation Bonds due in annual installments ranging from \$5,000 to \$20,000 through July 1, 2031, plus interest at 6.50%.	240,000
\$430,000 General Obligation Note Serial 2003-04 payable in annual installments of \$70,000 and \$75,000 through July 1, 2010, plus interest based on LIBOR at 90 days plus 1.25%	75,000
\$1,510,000 General Obligation Notes Serial 2003-04 payable in annual installments ranging from \$150,000 to \$195,000 through July 1, 2014 plus interest based on LIBOR at 90 days plus 1.25%.	715,000
\$535,000 general obligation bond serial 2008-2009 payable in annual installments ranging from \$65,000 to \$10,000 through July 1, 2014 plus interest based on LIBOR at 90 days plus 1.25%.	<u>410,000</u>
	<u><b>\$3,975,000</b></u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**10. LONG-TERM DEBTS (CONTINUED)**

The annual debt service requirements to maturity bonds and notes payables of June 30, 2010 are as follows:

**Governmental –type Activities:**

<u>Year ended June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Aggregate Obligation</u>
2011	\$ 297,000	\$ 263,363	\$ 560,363
2012	405,000	256,359	661,359
2013	425,000	232,342	657,342
2014	454,000	206,891	660,891
2015	495,000	179,431	674,431
2016-2020	804,000	686,597	1,490,597
2021-2025	675,000	435,069	1,110,069
2026-2030	805,000	206,548	1,011,548
2031-2032	<u>215,000</u>	<u>8,288</u>	<u>223,288</u>
	<u>\$4,575,000</u>	<u>\$2,474,888</u>	<u>\$7,049,888</u>

**Business-type activities:**

Mortgage note is payable in monthly installments of \$6,566 through 2019.

Mortgage payable consist of permanent residence loans provided by USDA–Rural Development. The land and building of the Project the mortgage note.

Mortgage note payable matures as follows:

<u>Year ended June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Aggregate Obligation</u>
2011	\$ 44,869	\$ 33,922	\$ 78,791
2012	48,593	30,198	78,791
2013	52,626	26,165	78,791
2014	56,994	21,797	78,791
2015	61,724	17,067	78,791
2016-2018	<u>259,258</u>	<u>16,510</u>	<u>275,768</u>
	<u>\$524,064</u>	<u>\$145,659</u>	<u>\$669,723</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**10. LONG-TERM DEBTS (CONTINUED)**

**Advances from CRIM and PR Treasury Department**

These amount represents the balance owed to CRIM as described in Note 3 and is payable in an of \$7,276 thereafter including interest at 6.2%. The advances from CRIM and PR Treasury Department mature as follows:

<u>Year ended June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Aggregate Obligation</u>
2011	\$ 6,401	\$ 11,178	\$ 17,579
2012	6,526	10,778	17,304
2013	6,660	10,371	17,031
2014	6,801	9,955	16,756
2015	6,951	9,531	16,482
2016-2020	36,567	42,078	78,645
2021-2024	42,200	29,929	72,129
2025-2029	43,381	15,893	59,274
2030-2032	<u>28,309</u>	<u>1,882</u>	<u>30,191</u>
	<u>\$183,796</u>	<u>\$141,595</u>	<u>\$325,391</u>

**11. RETIREMENT SYSTEM:**

**Defined Benefit Pension Plan**

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**11. RETIREMENT SYSTEM (CONTINUED)**

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

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

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

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

**Defined Contribution Plan**

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**11. RETIREMENT SYSTEM (CONTINUED)**

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

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

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

Total employees and employer contributions to the above mentioned plans during the year ended June 30, 2010 amounted to approximately \$187,077 and \$173,741, respectively. This amount represented 100% of the required contribution for the corresponding year.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2010, a copy of which can be obtained from the Retirement System.

**12. CONTINGENCIES**

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

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**JUNE 30, 2010**

**13. MUNICIPAL LANDFILL**

State and federal laws and regulations requires to the Municipality to carry out certain closure work when it stops accepting waste and to perform certain maintenance and monitoring functions at site in the following years. In accordance with GASB No. 18 "Accounting for Municipal Solid Waste Landfill Closure and Post Closure Care Costs" the Municipality must has to perform a study of the closing and post closing costs in order to recognize a provision for those costs.

The Municipality operated a solid waste landfill that was closed during 1994. Total closure costs incurred as of June 30, 2010 were approximately \$1,300,000. The closure costs incurred were mostly provided by federal awards under the State Block Grant Program.

The Municipality is still in process of performing tests in the landfill site in order to assess a final settlement of closure and post-closure costs. A preliminary estimate of these costs as of June 30, 2010 amounted to \$1,360,000. Accordingly, a provision for future closure and post closed costs was recognized in the accompanying financial statements.

**REQUIRED SUPPLEMENTARY INFORMATION**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF BUDGETARY COMPARISON  
FOR THE YEAR ENDED JUNE 30, 2010**

GENERAL FUND				
	<u>ORIGINAL BUDGET</u>	<u>AMMENDED BUDGET</u>	<u>ACTUAL</u>	<u>VARIANCE WITH FINAL BUDGET FAVORABLE (UNFAVORABLE)</u>
<b>Revenues:</b>				
Taxes:				
Property taxes	\$6,152,827	\$6,152,827	\$6,154,326	\$ 1,499
Municipal tax	650,000	650,000	689,933	39,933
Licenses and permits	503,000	503,000	123,270	(379,730)
Interest	180,000	180,000	43,185	(136,815)
Rent	90,000	90,000	107,022	17,022
Grants and entitlements	818,000	818,000	812,773	(5,227)
Other	<u>428,000</u>	<u>428,000</u>	<u>400,453</u>	<u>(27,547)</u>
Total revenues	<u>8,821,827</u>	<u>8,821,827</u>	<u>8,330,962</u>	<u>(490,865)</u>
<b>Expenditures:</b>				
General administration	3,550,168	3,544,354	3,448,486	95,868
Public safety	715,145	706,487	624,753	81,734
Education, culture and recreational	768,421	781,364	768,864	12,500
Public works and sanitation	2,429,881	2,387,935	2,337,171	50,764
Cultural and Tourist Development	251,186	277,588	274,877	2,711
Economic Development	180,010	179,010	167,643	11,367
Family and Social Development	872,143	892,216	844,286	47,930
Planning	<u>54,873</u>	<u>52,873</u>	<u>17,526</u>	<u>35,347</u>
Total expenditures	<u>8,821,827</u>	<u>8,821,827</u>	<u>8,483,606</u>	<u>338,221</u>
<b>Excess of expenditures over revenues</b>	<u>\$ _____</u>	<u>\$ _____</u>	<u>\$ (152,644)</u>	<u>\$(152,644)</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO SCHEDULE OF BUDGETARY COMPARISON**  
**JUNE 30, 2010**

**1. BUDGETS AND BUDGETARY ACCOUNTING**

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

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

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

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO SCHEDULE OF BUDGETARY COMPARISON**  
**JUNE 30, 2010**

**2. RECONCILIATION OF GAAP TO BUDGETARY BASIS**

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

Excess of expenditures over revenues, budgetary basis	\$(152,644)
Adjustments to accounts payable and accrued expenses	(466,389)
Adjustments to accounts receivable	<u>500,932</u>
Excess of revenues and other financial sources under expenditures and other financial sources per generally accepted accounting principle	<u>\$(118,101)</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2010**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
YEAR ENDED JUNE 30, 2010**

	<u>NUMBER</u>	<u>DISBURSEMENT</u>
<b><u>US Department of Housing and Urban Development</u></b>		
Passed through:		
Municipal Service Administration:		
Community Development Block Grant	14.228	\$ 692,079
ARRA - Community Development Block Grant	14.225	<u>242,142</u>
		934,221
Direct Program:		
Section 8- Housing Choice Vouchers	14.871	440,785
Supportive Housing Program	14.235	<u>51,653</u>
		<u>1,426,659</u>
<b><u>US Department of Agriculture</u></b>		
Passed through:		
PR Department of Education:		
Child and Adult Food Program	10.558	<u>52,814</u>
<b><u>US Department of Health and Human Services</u></b>		
Passes through:		
PR Department of Family:		
Child Care and Development Block Grant	93.575	589,547
ARRA – Child Care and Development Block Grant	93.713	<u>28,935</u>
		<u>618,482</u>
<b><u>US Department of Homeland and Security</u></b>		
Passes through:		
PR Office of Management and Budget (GAR)		
Public Assistance Grant	97.036	153,056
PR Department of Justice		
Homeland Security Grant Program	97.067	<u>24,234</u>
		<u>177,290</u>
		<u>\$2,275,245</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**JUNE 30, 2010**

**1. BASIS OF PRESENTATION:**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Municipality of Aguas Buenas, Puerto Rico and is prepared on the modified accrual basis of accounting. Accordingly, amounts presented in the accompanying schedule agree to amounts presented in the basic financial statements.

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

*Carlos R. Diaz Negrón*

Certified Public Accountant

MEMBER:

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

PO BOX 408, RAFAEL LASA NO. 44, AGUAS BUENAS, PR 00703 – TEL: 787-732-8020 – FAX: 787-732-0685 - E-MAIL: [oficinacarlosdiazcpa@yahoo.com](mailto:oficinacarlosdiazcpa@yahoo.com)

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

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

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Municipality of Aguas Buenas, Puerto Rico, as of and for the year ended June 30, 2010, which collectively comprise the Municipality of Aguas Buenas, Puerto Rico's basic financial statements and have issued our report thereon dated November 22, 2010. Other auditors audited the financial statements of The Espiritu Santo Project, as described in our report on Municipality of Aguas Buenas, Puerto Rico's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting of compliance and other matters that are reported on separately by those auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered Municipality of Aguas Buenas, Puerto Rico's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Municipality of Aguas Buenas, Puerto Rico's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Municipality of Aguas Buenas, Puerto Rico's internal control over financial reporting.

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

## REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING (CONTINUED)

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting. Finding 01-10. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

### Compliance and Other Matters

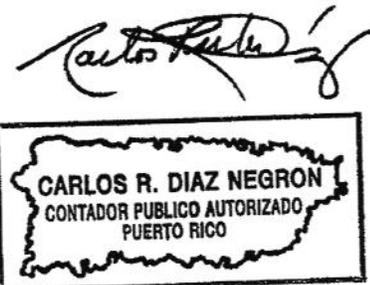
As part of obtaining reasonable assurance about whether Municipality of Aguas Buenas, Puerto Rico's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 01-10.

We noted certain matters that we reported to management of Municipality of Aguas Buenas, Puerto Rico, in a separate letter dated November 22, 2010.

This report is intended solely for the information and use of management, City Council, others within the entity, 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.

November 22, 2010  
Aguas Buenas, Puerto Rico

License No. 1339  
Expires December 1, 2013



The stamp No. **2564396** of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

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

*Carlos R. Diaz Negrón*

Certified Public Accountant

MEMBER:

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

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

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

**Compliance**

We have audited the compliance of **Municipality of Aguas Buenas, 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, 2010. Municipality of Aguas Buenas, Puerto Rico'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 Aguas Buenas, Puerto Rico's management. Our responsibility is to express an opinion on Municipality of Aguas Buenas, Puerto Rico's compliance based on our audit.

Municipality of Aguas Buenas, Puerto Rico's basic financial statements include the operations of Espiritu Santo Project, which expensed \$766,431 in federal awards which is not included in the schedule during the year ended June 30, 2010. Our audit described below did not include the operations of Espiritu Santo Project because Municipality of Aguas Buenas, Puerto Rico engaged other auditors to perform an audit in accordance with OMB A-133.

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 Aguas Buenas, Puerto Rico'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 Aguas Buenas, Puerto Rico's compliance with those requirements.

## REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE (CONTINUED)

As described in items 02-10 to 06-10 in the accompanying schedule of findings and questioned cost the Municipality of Aguas Buenas, Puerto Rico did not comply with the following requirements:

<u>Finding</u>	<u>Federal Program</u>	<u>Type of Compliance Requirement</u>
02-10	14.871 Housing Choice Voucher	Special test and provision
03-10	14.871 Housing Choice Voucher	Special test and provision
04-10	14.228 Community Development Block Grant	Davis Bacon Act
05-10	14.228 Community Development Block Grant	Procurement Supervision and Debarment
06-10	14.228 Community Development Block Grant	Allowed Cost, Cost Principle

Compliance with such requirements is necessary in our opinion for Municipality of Aguas Buenas, Puerto Rico to comply with the requirement applicable.

In our opinion, except for the non compliances in the preceding paragraph, Municipality of Aguas Buenas, 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, 2010.

### Internal Control Over Compliance

Management of Municipality of Aguas Buenas, 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 Aguas Buenas, Puerto Rico's internal control over compliance with the 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 internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality of Aguas Buenas, Puerto Rico's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE (CONTINUED)**

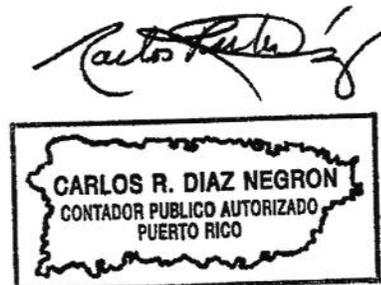
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, of material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identify certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying schedule of findings and questions costs as item 02-10 to 06-10. A significant deficiency in internal control over compliance is a deficiency, of a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Municipality of Aguas Buenas, Puerto Rico's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Municipality of Aguas Buenas, Puerto Rico's responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of management, City Council, others within the entity, 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.

November 22, 2010  
Aguas Buenas, Puerto Rico

License No. 1339  
Expire December 1, 2013



The stamp No. **2564397** of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2010**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2010**

**SECTION I - SUMMARY OF AUDITOR'S RESULTS**

**Financial Statements**

Type of auditor's report issued

Unqualified

Internal control over financial reporting:

- Material weakness identified? \_\_\_yes    Xno
- Significant deficiency identified that is not considered to be material weaknesses? Xyes    \_\_\_no

Noncompliance material to financial statement noted? \_\_\_yes    Xno

**Federal Awards**

Internal control over major programs:

- Material weakness identified? \_\_\_yes    Xno
- Significant deficiency identified that are not considered to be material weakness? Xyes    \_\_\_no

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

Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133 Xyes    \_\_\_no

Identification of major programs:

CFA Number(s)

Name of Federal Program

14.871

Section 8 – Housing Choice Voucher

14.228

Community Development Block Grants

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

\$300,000

Audit qualified as low-risk audited? \_\_\_yes    Xno

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2010**

**SECTION II - FINANCIAL STATEMENT FINDINGS**

**Finding No. 01-10 - Municipal Solid Waste Landfill GASB 18**

The estimated liability and the related disclosure presented in the financial statement related to costs of closure and postclosure of the Municipal solid waste landfill is not based on actual engineering studies. Therefore, we were unable to obtain a reliable base on which those estimates were based. Management believes that the effect in the June 30, 2006 financial statements is not material. However, as years going by the accrual will be material and the amount must be based on reliable sources.

We recommend performing the engineering studies to determine the factors necessary to calculate the amount to be accrued for cost closure and postclosure care. These costs include the following:

- The cost of equipment expected to be installed and facilities expected to be constructed near or after the date the landfill stops accepting waste and during the postclosure period. Such equipment might include gas monitoring and collection systems, storm water management systems, and groundwater monitoring wells.
- The cost of final cover (i.e., capping) expected to be applied near or after the closure date.
- The cost of monitoring and maintaining the expected usable landfill area during the postclosure period.

The amount to be accrued each period should be determined using a depletion approach and should be based on the percentage of capacity used during the period.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 02-10 – HQS Enforcement**

**Federal program**

CFDA No. 14.871 – Housing Choice Voucher

**Compliance requirement:**

Special Tests and Provisions – HQS Enforcement

**Category:**

Compliance

**Condition:**

During our examination, we selected 9 participants' file to test compliance with housing quality standard requirement. One of the file did not contain a unit re-inspections report or evidence of verification of the documentation that on PHA requirements was complete. The PHA did not properly stopped the HAP's or terminate HAP contract.

**Criteria:**

24 CFR sections 982.158 (d) and 982.404 establish that the PHA must prepare a unit inspection report. If the owner fails to maintain the dwelling unit in accordance with HQS, the PHA must take prompt and vigorous action to enforce the owner obligations. PHA remedies for such breach of the HQS include termination, suspension or reduction of housing assistance payments and termination of the HAP contract. The PHA must not make any housing assistance payments for a dwelling unit that fails to meet the HQS, unless the owner corrects the defect within the period specified by the PHA and the PHA verifies the correction. If a defect is life threatening, the owner must correct the defect within no more than 24 hours. For other defects, the owner must correct the defect within no more than 30 calendar days (or any PHA-approved extension).

**Effect:**

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 02-10 – HQS Enforcement**

**Questioned cost:**

None

**Recommendation:**

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 03-10 – Depository Agreements – Section 8**

**Federal program**

CFDA No. 14.871 Housing Choice Voucher

**Compliance requirement:**

Special Tests and Provisions – Depository Agreements

**Category:**

Compliance

**Condition:**

The municipality does not maintain a depository agreements with their financial institution in the form require by HUD.

**Criteria:**

**24 CFR Section 982.156 requires that:**

- a) Unless otherwise required or permitted by HUD, all program receipts must be promptly deposited with a financial institution selected as depository by the PHA in accordance with HUD requirements.
- b) The PHA may only withdraw deposited program receipts for use in connection with the program in accordance with HUD requirements.
- c) The PHA must enter into an agreement with the depository in the form required by HUD.
- d) (1) If required under written freeze notice form HUD to the depository may not permit any withdrawal by the PHA of funds held under the depository agreement unless expressly authorized by written notice form HUD to the depository; and (ii) The depository must permit withdrawals of such funds by HUD.  
  
(2) HUD must send the PHA a copy of the freeze notice form HUD to the depository. (Approved by the Office of Management and Budget under control number 25770169) [60 FR 34695, July 3, 1995, as amended at 60 FR 45661, Sept. 1, 1995]

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 03-10 – Depository Agreements – Section 8**

**Effect:**

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

**Questioned cost:**

None

**Recommendation:**

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

**SECTION III - FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS**

**Finding No. 04-10 – Davis Bacon Act**

**Federal Program**

CFDA - 14.228 Community Development Block Grant

**Compliance requirement:**

Davis – Bacon Act

**Category:**

Compliance/internal control

**Condition:**

As part of our audit procedures we tested 13 disbursements to test the compliance with the Davis-Bacon Act for Public Assistance Grants Program. In 5 of the 5 disbursements amounting \$557,265,681 the related contracts do not state that the contractor must comply with the requirement the David-Bacon Act. In 1 of the 5 the contractors did not submit the payrolls to the Municipality for examination.

**Criteria:**

Section 40 USC 3141-3144, 346 and 347 state that when required by the Davis Bacon Act, the Department of labor's (DOL) government wide implementation of the Davis-Bacon Act, or by Federal program legislation, all labor and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by Federal Assistance Fund must be paid wages not less than those established for the locality of the project (prevailing wage rate) by de DOL.

Non-federal entities shall include in their construction contracts subject to the Davis-Bacon Act a requirement that the contractor or subcontractor comply with the requirements of the Davis-Bacon Act and the DOL regulations (29 CFR part 5, "Labor Standards Provisions Applicable to Contacts Governing Federally Financed and Assisted Construction"). This includes a requirement for the contractor or subcontractor to submit to the non-Federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payrolls) (29 CFR sections 5.5 and 5.6). This reporting is often done using Optional Form WH-347 which includes the required statement of compliance (OMB No. 1215-0149).

**Effect:**

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 04-10 – Davis Bacon Act**

**Questioned cost:**

None

**Recommendation:**

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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 05-10 – Procurement and Suspension and Debarment**

**Federal Program**

CFDA – 14.228 Community Development Block Grant

**Compliance requirement:**

Procurement and Suspension and Debarment

**Category:**

Compliance

**Condition:**

As part of our audit procedures we tested 13 disbursements to test the compliance with the Procurement and Suspension and Debarment requirement for Community Development Block Grant program. In 9 of the 9 disbursements amounting \$688,470.50 the Municipality did not comply with Suspension and Debarment requirement.

**Criteria:**

Suspension and Debarment:

2 CFR part 180 states that non-federal entities are prohibited from contracting with or making subawards under covered transactions to parties that are suspended or debarred or whose principals are suspended or debarred. Covered transactions include those procurement contracts for goods and services awarded under a nonprocurement transaction (e.g., grant or cooperative agreement) that are expected to equal or exceed \$25,000 or meet certain other specified criteria. CFR section 180.220 of the government-wide nonprocurement debarment and suspension guidance contains those additional limited circumstances. All nonprocurement transactions (i.e., subawards to subrecipients), irrespective of award amount, are considered covered transactions.

When a non-federal entity enters into a covered transaction with an entity at a lower tier, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded. This verification may be accomplished by checking the Excluded Parties List System (EPLS) maintained by the General Services Administration (GSA), collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 05-10 – Procurement and Suspension and Debarment**

**Effect:**

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

**Questioned cost:**

None

**Recommendation:**

We recommend that the Municipality establishes an adequate internal control system to ascertain compliance with the Procurement and Suspension and Debarment requirement.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AGUAS BUENAS**  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)**  
**FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 06-10 – Allowed Cost, Cost Principles**

**Federal program**

CFDA No. 14.228 – Community Development Clock Grant

**Compliance requirement:**

Allowed Cost, Cost Principles

**Category:**

Compliance

**Condition:**

During our examination, we noted that the CDBG accountant is paid with CDBG finds but performs multiple activities not related to the CDBG program.

**Criteria:**

Circular A-87, attachment B, Paragraph 11 these standards regarding time distribution are in addition to the standards for payroll documentation.

- (1) Charges to Federal awards for salaries and wages, whether treated as direct or indirect costs, will be based on payrolls documented in accordance with generally accepted practice of the governmental unit and approved by a responsible official(s) of the governmental unit.
- (2) No further documentation is required for the salaries and wages of employees who work in a single indirect cost activity.
- (3) Where employees are expected to work solely on a single Federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications will be prepared at least semi annually and will be signed by the employee or supervisory official having first hand knowledge of the work performed by the employee.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE YEAR ENDED JUNE 30, 2010**

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

**Finding No. 06-10 – Allowed Cost, Cost Principles**

**Criteria:**

- (4) Where employees work on multiple activities or cost objectives, a distribution of their salaries or wages will be supported by personnel activity reports or equivalent documentation which meets the standards in subsection (5) unless a statistical sampling system or other substitute system has been approved by the cognizant Federal Agency. Such documentary support will be required where employees work on:
- (a) More than one Federal award,
  - (b) A Federal award and a non Federal award,
  - (c) An indirect cost activity and a direct cost activity,
  - (d) Two or more indirect activities which are allocated using different allocation bases, or
  - (e) An unallowable activity and a direct or indirect cost activity.

**Effect:**

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

**Questioned costs:**

None

**Recommendation:**

We recommend that the Municipality after the required documentation returns the funds to the program section and establish an adequate internal control system to ascertain compliance with the requirements of the program.

**Management expense:**

See accompanying management's response.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AGUAS BUENAS**

**EXHIBIT – I**

**CORRECTIVE ACTION PLAN  
FOR YEAR ENDED JUNE 30, 2010**



**DEPARTAMENTO DE FINANZAS Y PRESUPUESTO**

**CORRECTIVE ACTION PLAN  
 SINGLE AUDIT FOR THE YEAR ENDED JUNE 30, 2010**

**Finding No. 01-10 Municipal Solid Waste Landfill GASB 18**

PROGRAM DEFICIENCY	OBJECTIVES	KEY TASK/ ACTION ITEMS	OBSTACLES	RESOURCES	LEAD STAFF NAME AND POSITION	COMPLETION TARGET DATE	ACTUAL COMPLETION DATE	IMPLEMENTATION PROGRESS COMMENTS
The estimated liability and related disclosure presented in the financial statement related to engineering studies. Therefore, we were unable to obtain a reliable base on which of those estimates were based. Management believes that the effect in June 30, 2006 financial statements is not material. However, these years going by the accrual will be material and the amount must be on reliable sources.	Closing of landfill	The Municipality has quoted the cost of closing the Landfill recently which the estimated cost is \$241,000.00. These funds available are \$314,500.00 CDBG to have the landfill post closed.	Lack of follow up on funds. None approval of funds.	The Earth Group Link	José Ortiz Federal Programs Accountant (787) 732-2811	December 15, 2010	March 15, 2011	The project was revised and the funds needed to finish was \$136,000.00. The difference of 314,500.00, \$178,000.00 was transfer to the project Street Paviment and was paid. The funds of 2001 was empty and the Municipality begin the closing process.



**DEPARTAMENTO DE FINANZAS Y PRESUPUESTO**

**Finding No. 02-10 HQS Enforcement**

PROGRAM DEFICIENCY	OBJECTIVES	KEY TASK/ ACTION ITEMS	OBSTACLES	RESOURCES	LEAD STAFF NAME AND POSITION	COMPLETION TARGET DATE	ACTUAL COMPLETION DATE	IMPLEMENTATION PROGRESS COMMENTS
The Municipality did not comply with the 24 CFR Sections 982.158(d) and the 982.404 that established that the PHA must prepare a unit inspections report and enforced in case the unit does not comply with HQS regulations.	Comply with 24 CFR Section 982.158 and 982.404	Establish an adequate internal control system to ascertain compliance with the requirements of the program. The internal control system should include at least that file should be revised the internal audit department.	Due to the turn over of the Housing Director and lack of Knowledge.	24 CFR Sections 982.158 and 982.404  HUD's Assistance	Norberto Rodriguez Housing Director (787)732-4185  Ivonne N. Laboy Special Projects Coordinator (787)732-4185	02/01/2011	01/21/2011	Due to the turn over of the Housing Directors the agency had poor control of this area. On May 2010 a Special Project Coordinator was assign to the PHA and all HQS Enforcement inspections has been done in a timely basis since then. The evidence was sent to HUD on October 19, 2010. We still waiting for HUD clearance of this. Attached copy of evidence sent to HUD.  An internal control system was implemented. All files are revised by the Quality Control Officer before processing them in order to comply with all required documentation.



**DEPARTAMENTO DE FINANZAS Y PRESUPUESTO**

**Finding No. 03-10 - Depository Agreements – Section 8**

PROGRAM DEFICIENCY	OBJECTIVES	KEY TASK/ ACTION ITEMS	OBSTACLES	RESOURCES	LEAD STAFF NAME AND POSITION	COMPLETION TARGET DATE	ACTUAL COMPLETION DATE	IMPLEMENTATION PROGRESS COMMENTS
The Municipality did not maintain a depository agreements with their financial institution in the form require by HUD.	Comply with 24 CFR Section 982.156		Lack of Knowledge	24 CFR Section 982.156	Norberto Rodriguez Housing Director (787) 732-4185  Ivonne N. Laboy Special Project Coordinator (787) 732-4185	02/01/2011	01/21/2011	The General Depository Agreement was formalized between the Municipality of Aguas Buenas and the Financial Institution as required by HUD. See copy attached.



**DEPARTAMENTO DE FINANZAS Y PRESUPUESTO**

**Finding No. 04-10 Davis Bacon**

PROGRAM DEFICIENCY	OBJECTIVES	KEY TASK/ ACTION ITEMS	OBSTACLES	RESOURCES	LEAD STAFF NAME AND POSITION	COMPLETION TARGET DATE	ACTUAL COMPLETION DATE	IMPLEMENTATION PROGRESS COMMENTS
The Municipality is responsible to comply with the Davis Bacon Act of the Department of Labor.	This includes a requirement for the contractor or subcontractors comply with the requirements of the Davis Bacon Act and the DOL regulations (29 CFR part 5, Labor Standards Provision Applicable to Contracts Governing subcontractor to submit to the non-Federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance ( certified payrolls)(29 CFR sections 5.5 and 5.6)This reportis often done using Optional Frm WH-347 which includes the required statement of compliance (OMB No. 1215-0149.	The correct contract form including the new clause regarding the Davis Bacon Act will be give to the Secretary's Office in order to comply with this requirement. This has to be used in future contracts.	The Municipality could be exposed to administrative action by the grantor. Lack of understanding.	Davis Bacon Act from the Department of Labor (40 USC 327-330)  24 CFR 85.36  29 CFR Part 3 and 5 from the Department of Labor	Norberto Rodriguez Special Projects Coordinator (787) 732-4185  David Pérez Administrative Assistant (787) 732-4185  Rosa Aponte Municipality's Secretary (787) 732-8621	February 22, 2011	February 22, 2011	After January 2010 all contracts with CDBG funds include the clause on comply with the Davis Bacon Act. Also, the contracted companies submit to the Federal Program Office the payroll of their employees and our Administrative Assistant David Perez realize the requirement interviews to the workers during the project.



**DEPARTAMENTO DE FINANZAS Y PRESUPUESTO**

**Finding No. 05-10 - Procurement and Suspension and Debarment**

PROGRAM DEFICIENCY	OBJECTIVES	KEY TASK/ ACTION ITEMS	OBSTACLES	RESOURCES	LEAD STAFF NAME AND POSITION	COMPLETION TARGET DATE	ACTUAL COMPLETION DATE	IMPLEMENTATION PROGRESS COMMENTS
The Municipality did not comply with the Procurement and Suspension and Debarment Act	Comply with this Law	The correct contract form including the new clause regarding the Procurement and Suspension and Debarment Act will be given to the Secretary's Office in order to comply with this requirement. This has to be used in future contracts. A General Service Administration (GSA) certification will be requested prior to the signature of the contract. This verification may be accomplished by checking the Excluded Parties list System (EPLS).	The Municipality could be exposed to administrative action by the grantor.  Lack of Knowledge	Excluded Parties List System (EPLS) from General Services Administration	Norberto Rodriguez Special Projects Coordinator (787) 732-4185  David Pérez Administrative Assistant (787) 732-4185  Rosa Aponte Municipality's Secretary (787) 732-8621	March 30, 2011	Pending	A copy of the contract will be send to the Municipality Secretary's Office including the new clause in order to comply with this requirement. Evidence will be submitted as soon as this is done.



**DEPARTAMENTO DE FINANZAS Y PRESUPUESTO**

**Finding No. 06-10 Allowed Cost, Cost Principles**

PROGRAM DEFICIENCY	OBJECTIVES	KEY TASK/ ACTION ITEMS	OBSTACLES	RESOURCES	LEAD STAFF NAME AND POSITION	COMPLETION TARGET DATE	ACTUAL COMPLETION DATE	IMPLEMENTATION PROGRESS COMMENTS
The CDBG Accountant is paid with CDBG funds but performs multiple activities not related to the CDBG program.	Comply with this principle. Circular A-87 attachment B Paragraph 11 these standards regarding time distribution are in addition to the standards for payroll documentation.	A prorated salary will be established to adjust the salary of the accountant.	This may result in the disallowance of program cost and the ability to manage federal awards in compliance with laws, regulations, and provisions of contract grants awarded could also be questioned.	24 CFR Section 984.305 (FSS Accounts)  HUD's Technical Assistance	Norberto Rodriguez Special Projects Coordinator (787) 732-4185  David Pérez Administrative Assistant (787) 732-4185  Rosa Aponte Municipality's Secretary (787) 732-8621	July 1, 2010	July 1, 2010	The accountant salary will be prorated to determine the time that works to other activities and the time that works with the CDBG program. After July 1, 2010 CDBG program submitted an invoice for the time dedicated to other activities not related to the CDBG program.

José A. Ortiz López  
Accountant

David Pérez  
Administrative Assistance