

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES**

**AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL**

**AREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE AÑASCO**  
**AUDITORIA 2002-2003**

**30 DE JUNIO DE 2003**

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**COMMONWEALTH OF PUERTO RICO**

**MUNICIPALITY OF AÑASCO  
BASIC FINANCIAL STATEMENTS**

**FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
Basic Financial Statements  
June 30, 2003**

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*Kenneth Vargas*

**CERTIFIED PUBLIC ACCOUNTANT**

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**Independent Auditor's Report**

The Honorable Mayor, Members of the  
Municipal Legislature and People of  
the Municipality of Añasco  
Añasco, Puerto Rico

I have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Añasco of the Commonwealth of Puerto Rico (the "Municipality"), as of and for the year ended June 30, 2003, which collectively comprise the Municipality's basic financial statements as listed in the accompanying table of contents. I also have audited the accompanying statements of revenues and expenditures, budget and actual-budgetary basis, general fund of the year ended, which is presented as part of the basic financial statements. These financial statements are the responsibility of the Municipality's management. My responsibility is to express an opinion on these financial statements based on my audit.

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

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Añasco of the Commonwealth of Puerto Rico, as of June 30, 2003, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America. In addition, in my opinion, the financial statements referred to above present fairly, in all material respects, the budgetary comparison of the general fund for the year ended in conformity with the budgetary (statutory) basis of accounting as describe in note 1.

As described in Note 1, on July 1, 2002 the Municipality implemented a new financial reporting model required by GASB Statement No. 34 (GASB No. 34), *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. In conjunction with the adoption of GASB No. 34, the Municipality has also adopted the following pronouncements: (1) GASB Statement No. 33 - *Accounting and Financial Reporting for Nonexchange Transactions*, (2) GASB Statement No. 37 - *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, (3) GASB Statement No. 38 - *Certain Financial Statement Note Disclosures*, and, (4) GASB Interpretation No. 6 - *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

Furthermore, in conjunction with the adoption of GASB No. 34, the Municipality adopted the following pronouncements for its governmental activities reported in the government-wide financial statements: (1) APB Opinion No. 20 – *Accounting Changes*, (2) APB Opinion No. 21 - *Interest on Receivables and Payables*, (3) FASB Statement No. 5 - *Accounting for Contingencies*, and (4) FASB Statement No. 16 – *Prior Period Adjustments*. Those pronouncements do not conflict with or contradict any GASB pronouncements adopted by the Municipality.

The accompanying Management's Discussion and Analysis and the Schedule of Funding Progress – Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities are not required parts of the basic financial statements referred to above, but are supplementary information required by accounting principles generally accepted in the United States of America. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, I did not audit the information and express no opinion on it.



Kenneth Vargas  
License 2251

Aguadilla, Puerto Rico  
January 26, 2004

Stamp No. 1688094 of the Puerto Rico  
Society of Certified Public Accountants  
was affixed to the record copy of this report.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Management's Discussion and Analysis  
Year Ended June 30, 2003

Management of the Municipality of Añasco of the Commonwealth of Puerto Rico (the Municipality) provides this *Management's Discussion and Analysis* (MD&A) for the readers of the Municipality's basic financial statements. This narrative represents an overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2003. Because this MD&A is designed to focus on the current year activities, resulting changes and currently known facts, we encourage readers to consider the information presented in this MD&A in conjunction with the additional information furnished in the accompanying basic financial statements.

During fiscal year ended June 30, 2003, the Municipality implemented the new required financial reporting standards established by Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, issued by the Governmental Accounting Standards Board (GASB No. 34). According to this statement, significant required changes in content and structure have been made in the accompanying basic financial statements as of and for the fiscal year ended June 30, 2003, which make them not easily comparable with prior years' financial statements. However, in future years, comparative analysis will be more meaningful and will go further in explaining the Municipality's financial position and results of operations.

**FINANCIAL HIGHLIGHTS**

**a) Government-Wide Highlights**

- **Assets** - The Municipality has reported assets amounting to \$37,485,398 in the accompanying statement of net assets, of which the most significant are capital assets, cash, short-term investments and accrued interest amounting to \$24,364,085, \$8,975,913 and \$2,893,883, respectively. These assets account for \$36,233,881 or 97% of the Municipality's total assets.
- **Liabilities** - The Municipality has reported liabilities amounting to \$25,968,682 in the accompanying statement of net assets, of which the most significant are bonds and notes payable, deferred revenues, landfill closure, and accounts payable amounting to \$10,929,750, \$4,408,410 and \$3,648,238, respectively. These liabilities account for \$18,986,398 or 73% of the Municipality's total liabilities.
- **Net assets** - The assets of the Municipality exceeded its liabilities by \$11,516,717 at June 30, 2003 which and is presented as "net assets" in the accompanying statement of net assets. Restricted net assets and unrestricted net liabilities amounted to \$3,499,055 and \$11,445,955, respectively. Net assets invested in capital assets amounted to \$19,463,616.
- **Net change in net assets** - The Municipality's net assets increased by \$2,650,852 (30% increase) during fiscal year ended June 30, 2003. Net assets at June 30, 2002 amounted to \$8,865,864. The increase in net assets represents a positive result of operations and an improvement in the Municipality's overall financial position in comparison with the prior fiscal year.
- **Revenues** - The Municipality has reported total revenues amounting to \$16,845,355 accompanying statement of activities, of which the most significant are tax revenues, capital grants and contributions and charges for services amounting to \$8,008,636, \$4,083,678 and

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\$2,566,454, respectively. These revenues account for \$14,658,768 or 87% of the Municipality's total revenues.

- **Expenses** - The Municipality has reported total expenses amounting to \$14,194,502 in the accompanying statement of activities, of which the most significant are categorized as general government; urban and economic development and health and sanitation amounting to \$5,425,376, \$3,498,512 and \$3,363,225, respectively. These expenses accounted for \$12,287,113 or 87% of the Municipality's total expenses.

**b) Governmental Funds Highlights**

- **Assets** - The Municipality's governmental funds have reported combined assets amounting to \$12,757,964 in the accompanying balance sheet – governmental funds, of which the most significant are cash, intergovernmental and taxes receivable amounting to \$8,975,913, \$2,694,085 and \$634,187, respectively. These assets account for \$12,231,157 or 96% of the Municipality's combined governmental funds assets.
- **Liabilities** - The Municipality's governmental funds have reported combined liabilities amounting to \$9,312,750 in the accompanying balance sheet – governmental funds, of which the most significant are deferred revenues, accounts payable and intergovernmental amounting to \$5,222,602, \$1,999,013 and \$1,508,173, respectively. These liabilities account for \$8,400,499 or 90% of the Municipality's combined governmental fund liabilities.
- **Governmental fund balances** - The Municipality's governmental funds reported combined fund balances amounting to \$3,445,215.
- **Net change in governmental fund balances** - The Municipality's governmental fund balances increased by \$1,203,353 (54% increases) during fiscal year ended June 30, 2003. Governmental fund balances at June 30, 2002, as restated, amounted to \$2,241,862.
- **Revenues** - The Municipality's governmental funds have reported combined revenues amounting to \$16,537,813 in the accompanying statement of activities, of which the most significant are tax revenues, intergovernmental grants and contributions and charges for services amounting to \$7,858,520, \$5,755,905 and \$2,473,339, respectively. These revenues account for \$16,087,764 or 97% of the Municipality's combined governmental fund revenues.

**Expenditures** - The Municipality's governmental funds have reported combined expenditures amounting to \$17,545,691 in the accompanying statement of activities, of which the most significant are categorized as general government; capital outlays, urban and economic development, and health and sanitation amounting to \$4,986,063, \$4,568,009, \$2,907,577 and \$2,805,164 respectively. These expenses accounted for \$15,266,813 or 87% of the Municipality's total expenses.

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## OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

This management's discussion and analysis is intended to serve as an introduction to the accompanying basic financial statements. The Municipality's basic financial statements include three components: (1) government-wide financial statements, (2) governmental fund financial statements, and (3) notes to the basic financial statements. This report also contains additional required and no required supplementary information in addition to the basic financial statements themselves. These components are described below.

The new basic financial statements are the result of a significant change in the focus of financial reporting in comparison with the financial statements previously issued by the Municipality. The new basic financial statements focus on: (1) the Municipality as a whole (government-wide financial reporting) and, (2) the Municipality's major individual governmental funds discussed below. Both perspectives (government-wide and major governmental fund financial reporting) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability. The components of the basic financial statements are described below.

### **a) Government-Wide Financial Statements**

The *government-wide financial statements* are designed to provide readers with a broad overview of the Municipality's operations and finance as a whole in a manner similar to private-sector business. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at June 30, 2003. These financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means that these financial statements follow methods that are similar to those used by most private businesses. They take into account all revenues and expenses connected with the fiscal year ended June 30, 2003 even if cash involved have not been received or paid. The government-wide financial statements are composed of: (1) the statements of net assets, and (2) the statement of activities.

#### **1. Statement of Net Assets**

The statement of net assets presents all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity). Over time, increases or decreases in the net assets may serve as a useful indicator of whether the financial position of the Municipality is either improving or deteriorating.

#### **2. Statement of Activities**

The statement of activities presents information showing how the Municipality's net assets changed during the fiscal year ended June 30, 2003. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and

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earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the Municipality.

Both of the abovementioned financial statements present all of the Municipality's governmental activities, which are supported mostly by taxes and intergovernmental revenues (such as federal and state grants and contributions). All services normally associated with the Municipality fall into this category, including culture, recreation and education, general government, health and sanitation, public safety, public housing and welfare, and economic and urban development. The government-wide financial statements can be found immediately following this management's discussion and analysis.

**b) Governmental Fund Financial Statements**

The Municipality's governmental fund financial statements consist of: (1) the balance sheet – governmental funds and (2) the statement of revenues, expenditures and changes in fund balances – governmental funds. These financial statements report the financial position and results of operations of the Municipality's governmental funds, with an emphasis on the Municipality's major funds.

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Municipality, like most other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Each fund is considered an independent fiscal entity accounted for within a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenue, and expenditures. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial and contractual provisions.

The governmental fund financial statements focus on: (1) individual parts of the Municipality's government and (2) reporting the Municipality's operations in more detail than the government-wide financial statements. For financial reporting purposes, the Municipality classifies its funds within the following fund categories: (1) general fund, (2) debt service fund, (3) nonmajor funds special revenue funds, and (4) capital projects funds.

Governmental funds are used to account for all of the services provided by the Municipality. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of expendable financial resources. They also focus on the balances of expendable financial resources available at the end of the fiscal year (June 30, 2003). This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Municipality's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Municipality, that is, evaluating the Municipality's near-term financing requirements. Both the governmental funds' balance sheet and the governmental funds' statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and the governmental activities reported in the government-wide financial statements.

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As previously mentioned, the Municipality has five major governmental funds. Each major fund is presented in a separate column in the governmental funds' balance sheet and the governmental funds' statement of revenues, expenditures and changes in fund balances. The five major governmental funds are: (1) the general fund, (2) the debt service fund, (3) \$1,850,000 bond Issuance fund, (4) SBGP and (5) Loan Section 108.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the fund information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Municipality's near-term financial decisions.

The Municipality has no activities that operate more like those of commercial enterprises nor have resources held for the benefit of parties outside the Municipality's government. Consequently, the Municipality has not reported proprietary funds or fiduciary funds in the accompanying basic financial statements. The governmental funds financial statements can be found immediately following the government-wide financial statements.

**c) Notes to Basic Financial Statements**

The notes to the basic financial statements provide additional information that is essential for a full understanding of the data provided in the government-wide and the governmental fund financial statements. The notes to the basic financial statements can be found immediately following the basic financial statements.

**d) Required Supplementary Information**

The basic financial statements are followed by a section of required supplementary information (RSI) which consists of a schedule of funding progress of the Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities (ERS). ERS is the retirement system in which the employees of the Municipality participate.

**e) Other Supplementary Information**

The RSI is followed by a section of no required supplementary information consisting of: (1) combining balance sheet - nonmajor governmental funds, (2) combining statement of revenues, expenditures and changes in fund balances - nonmajor governmental funds, (3) schedule of revenues and expenditures - budget and actual - budgeting basis - debt service fund, and (4) schedules of capital assets used in the operation of governmental funds, as detailed in the accompanying table of contents.

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**INFRASTRUCTURE ASSETS**

Historically, infrastructure assets, which are one of the Municipality's largest group of assets (consisting of roads, bridges, traffic signals, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in governmental financial statements. According to GASB No. 34, the Municipality has valued and reported infrastructure assets in the accompanying government-wide financial statements. Additionally, under the provisions of GASB No. 34, the Municipality had the option to either: (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity.

If the Municipality would have developed the asset management system (commonly known as the *modified approach*), then the Municipality would have to measure and demonstrate its maintenance of locally established levels of service standards at least every three years for each infrastructure asset category. Under the modified approach, the Municipality would have recorded its cost of maintenance in lieu of depreciation and amortization. As of July 1, 2002, the Municipality retroactively recorded the estimated historical costs of infrastructure assets in the accompanying government-wide financial statements. Also the Municipality elected to depreciate infrastructure assets instead of using the modified approach.

**GOVERNMENT-WIDE FINANCIAL ANALYSIS**

**a) Net Assets**

As noted earlier, net assets may serve over time as a useful indicator of the Municipality's financial position. Total assets and total liabilities at June 30, 2003 amounted to \$37,485,398 and \$25,968,682, respectively, for net assets of \$11,516,716, compared to net assets of \$8,865,864 at June 30, 2002.

The Municipality's net assets include net assets invested in capital assets amounting to \$19,463,616. The Municipality uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. The resources needed to repay this debt must be provided from other sources since the capital assets themselves cannot be used to liquidate these liabilities.

A portion of the Municipality's net assets amounting to \$3,499,099 represents resources that are subject to external restrictions on how they may be used. Restrictions on these resources are mainly related to: (1) the future acquisition or construction of capital assets, (2) the future payment of debt service.

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The following is a condensed presentation of the Municipality's financial position, as reported in the government-wide financial statements:

**Condensed Statement of Net Assets**  
**June 30, 2003**

	<b>Governmental Activities</b>
<b>Assets:</b>	
Current assets	\$ 13,049,904
Noncurrent assets:	
Capital assets, net	24,364,085
Other noncurrent assets	71,409
Total assets	\$ 37,485,398
 <b>Liabilities:</b>	
Current liabilities	\$ 9,591,381
Noncurrent liabilities - long-term liabilities due after one year	16,377,301
Total liabilities	\$ 25,968,682
 <b>Net assets (liabilities):</b>	
Invested in capital assets, net of related debt	\$ 19,463,617
Restricted	3,499,055
Unrestricted	(11,445,955)
Total net assets	\$11,516,717

The Municipality's current assets amounting to \$13,049,904 are mainly composed of restricted cash, intergovernmental and property taxes receivable amounting to \$8,975,913, \$2,893,883 and \$561,159, respectively. The restricted cash represents resources legally designated for the payment of debt service, the acquisition and construction of major capital assets, and resources designated for the operations of federal and state funded programs. Restricted cash also consist of unused proceeds of bonds issued to pay accounts payable and certain specific commitments, previously agreed with and approved by the Government Development Bank for Puerto Rico. The short-term investment in certificates of deposit is unrestricted and available to meet operational needs and obligations with citizens and creditors.

The Municipality's noncurrent assets amounting to \$24,435,494 are substantially composed of capital assets, net of accumulated depreciation and amortization, amounting to \$24,364,085.

The Municipality's current liabilities amounting to \$9,591,381 are mainly composed of deferred revenues, accounts payable, and the current portions of compensated absences and bonds and notes payable amounting to \$4,408,410, \$3,998,406, \$237,723 and \$849,967, respectively.

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Deferred revenues principally consist of unearned revenues associated with municipal license taxes and intergovernmental grants and contributions related to state and federal funded programs.

The Municipality's noncurrent liabilities amounting to \$16,377,301 are mainly composed of the long-term portions of bonds and notes payable and compensated absences amounting to \$11,635,618 and \$1,463,704, respectively.

As noted in the condensed statement of net assets, the Municipality's current assets exceeded current liabilities by \$11,516,717, for a current ratio (current assets to current liabilities) of 1.44 to 1.00.

**b) Changes in Net Assets**

The Municipality's net assets increased by \$2,658,853 or 30% from last year's total net assets. Approximately 55% of the Municipality's total revenues (\$16,845,355) come from property and municipal license taxes.

The Municipality's expenses cover a wide range of services. The largest expenses of the Municipality were related to: (1) general administration and operating costs (\$5,425,376), which were classified as "general government" and accounted for 38% of total expenses, (2) culture, recreation and education (\$338,194), which accounted for 2% of total expenses, (3) health and sanitation (\$3,363,225), which accounted for 24% of total expenses, (4) urban and economic development (\$3,498,578), which accounted for 25% of total expenses, and (5) public housing and welfare (\$937,327), which accounted for 7% of total expenses.

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**MUNICIPALITY OF AÑASCO**  
**Management's Discussion and Analysis**  
**Year Ended June 30, 2003**

The following is a condensed presentation of the Municipality's results of operations, as reported in the government-wide financial statements:

**Condensed Statement of Activities**  
**Year Ended June 30, 2003**

***Program revenues:***

Program-specific capital grants and contributions	\$ 4,083,678
Program-specific operating grants and contributions	426,561
Charges for services	2,566,454
Total program revenues	7,076,693

***General revenues:***

Property taxes	6,589,450
Municipal license taxes	1,419,186
Intergovernmental contributions and reimbursements	1,309,977
Unrestricted investment earnings	99,636
Other general revenues (various sources)	350,413
Total general revenues	9,768,662
Total revenues	16,845,355

***Program expenses:***

General government	5,425,376
Urban and economic development	3,498,512
Public safety	201,874
Health and sanitation	3,363,225
Culture, recreation and education	338,194
Public housing and welfare	937,327
Interest on long-term obligations	429,994
Total expenses	14,194,502

<b><i>Net increase in net assets</i></b>	2,650,853
<b><i>Net assets - at beginning of year</i></b>	8,865,864
<b><i>Net assets - at end of year</i></b>	\$ 11,516,717

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**Year Ended June 30, 2003**

Governmental activities increased the Municipality's net assets by \$2,650,853. A comparison of the cost of services by function for the Municipality's governmental activities is shown below, along with the revenue used to cover the net expenses of the governmental activities.

**Governmental Activities - Expenses Net of Program Revenues:**  
**Year Ended June 30, 2003**

***Net expenses:***

General government	\$ (1,085,516)
Urban and economic development	(2,445,788)
Public safety	( 201,874)
Health and sanitation	(1,939,256)
Culture, recreation and education	( 338,194)
Public housing and welfare	( 677,187)
Interest on long-term obligations	( 429,994)
Total governmental activities' net expenses	<u>( 7,117,809)</u>

***General revenues:***

Taxes	8,008,636
Unrestricted intergovernmental grants and contributions	1,309,977
Other revenues sources	450,049
Total governmental activities general revenues	<u>9,768,662</u>
Net increase in net assets	<u>\$ 2,650,853</u>

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**FINANCIAL ANALYSIS OF GOVERNMENTAL FUNDS**

As discussed earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of expendable 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.

At June 30, 2003, the Municipality's governmental funds reported combined fund balances of \$3,445,215, an increase of \$1,203,353 or 54% in comparison with the prior year. There are \$3,804,622 of reserved fund balances to indicate that are not available for new spending because have been already committed: (1) to liquidate contracts and purchase orders of the prior fiscal year (\$310,528), (2) to pay debt service (\$1,296,207), and (3) capital projects (\$2,197,887).

The general fund is the chief operating fund of the Municipality. At the end of the current fiscal year, unreserved fund deficit of the general fund was \$252,562, while its total fund balance reached \$57,966. The fund balance of the general fund decreased by \$754,309 due to the excess of revenues and other financing sources over expenditures and other financing uses.

Combined revenues of governmental funds for the year ended June 30, 2003 amounted to \$16,537,813, while total combined revenues for the prior year amounted to \$16,972,274. This represents a decrease of \$434,461 in comparison with the prior year.

The following table's presents a comparison of the individual revenue sources for fiscal years ended June 30, 2002 and 2003. Also, see additional related comments in the following section titled General Fund Budgetary Highlights.

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The following is a condensed presentation of the Municipality's balance sheet and results of operations of governmental funds:

**Condensed Balance Sheet - Governmental funds**  
**June 30, 2003**

<b>Assets:</b>	
Total assets - major funds	\$11,902,008
Total assets - nonmajor funds	855,956
Total assets	<u>12,757,964</u>
<b>Liabilities:</b>	
Total liabilities - major funds	8,705,693
Total liabilities - nonmajor funds	607,056
Total liabilities	<u>9,312,749</u>
<b>Fund Balances:</b>	
Reserved - major funds	3,448,877
Reserved - nonmajor funds	355,745
Unreserved - major funds	<u>(359,407)</u>
Total fund balances	<u>\$ 3,445,215</u>

**Condensed Statement of Revenues, Expenditures:**  
**and Changes in Fund Balances - Governmental Funds**  
Year Ended June 30, 2003

<b>Revenues:</b>	
Total revenues - major funds	\$15,533,317
Total revenues - nonmajor funds	1,004,306
Total revenues	<u>16,537,813</u>
<b>Expenditures:</b>	
Total expenditures - major funds	16,071,857
Total expenditures - nonmajor	1,473,834
Total expenditures	<u>17,545,691</u>
<b>Other financing sources (uses), net:</b>	
Major funds	1,863,347
Nonmajor funds	347,884
Total other financing sources (uses), net	<u>2,211,231</u>
<b>Excess of expenditures and other financing uses over</b>	
<b>revenues and other financing sources</b>	1,203,353
<b>Fund balance at beginning of year, as restated</b>	<u>2,241,862</u>
<b>Fund balance at end of year</b>	<u>\$ 3,445,215</u>

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Management's Discussion and Analysis  
Year Ended June 30, 2003

**BUDGETARY HIGHLIGHTS**

**a) General Fund**

The original budget and the final amended budget of the general fund remained substantially the same except for reclassification of expenditures made through the year. Over the course of the year, the Municipality revised the general fund'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 total actual revenues (budgetary basis) of the general fund for the fiscal year ended June 30, 2003 were \$10,200,177, which is \$1,228,153 less than the budgeted revenues.

The total actual expenditures (budgetary basis) of the general fund for the same year previously mentioned were \$10,577,904, which is \$850,426 more than the budgeted expenditures.

**CAPITAL ASSETS AND DEBT ADMINISTRATION**

**a) Capital Assets**

The accompanying statement of net assets reported total capital assets, at cost, amounting to \$40,910,327, of which \$12,093,052 represents infrastructure assets at June 30, 2003. The related accumulated depreciation and amortization of capital assets amounted to \$16,546,242 of which \$7,176,373 is related to infrastructure assets at June 30, 2003. The investment in capital assets includes land and land improvements, buildings and buildings improvements, machinery and equipment, licensed vehicles, furniture and fixtures, infrastructure and construction in progress.

The net book value of capital assets at June 30, 2003 is distributed by function/activity. Actual expenditures to purchase or construct capital assets were \$4,568,009 for the year.

The increase in net capital assets at June 30, 2003 in comparison with the respective figures at June 30, 2002 was \$3,432,683. Such increase is due to the net effect of the additions to capital assets amounting to \$4,568,009 made during the year, and the effect of depreciation and amortization expense of \$1,135,326.

**b) Debt Administration**

The Municipality finances a significant portion of its construction activities through bond issuances and through state and federal grants. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Management's Discussion and Analysis  
Year Ended June 30, 2003

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

The laws and regulations of the Commonwealth of Puerto Rico have 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 laws and regulations also require 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 projected by the Government Development Bank for Puerto Rico, 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 laws and regulations 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.

For more detailed information related to the capital assets and long-term debt activity for the year ended June 30, 2003, please refer to the accompanying notes to the basic financial statements.

#### **REQUEST FOR INFORMATION**

This financial report is designed to provide a general overview of the Municipality's finances for all of the Municipality's citizens, taxpayers, customers, investors and creditors. This financial report seeks to demonstrate the Municipality's accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to: Municipality of Añasco, Department of Finance, P. O. Box 945, Añasco, Puerto Rico, 00681.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Statement of Net Assets  
June 30, 2003

<b>Assets</b>	<b>Governmental activities</b>
<b>Current assets:</b>	
Cash with commercial banks:	\$ 937,418
Accounts receivable, net of allowance for doubtful accounts:	
Taxes:	
Property taxes	561,159
Municipal license taxes	73,028
Accrued interest	5,035
Intergovernmental	2,893,883
Other	447,633
Inventories and other current assets	93,253
<b>Restricted assets :</b>	
Cash with commercial banks, including cash equivalent \$1,021,291	4,397,478
Cash with fiscal agent	3,641,017
Total current assets	13,049,904
<b>Noncurrent assets:</b>	
Capital assets, net of accumulated depreciation and amortization of \$16,546,242	24,364,085
Deferred charges, net of accumulated amortization of \$25,119	71,409
Total noncurrent assets	24,435,494
Total assets	\$ 37,485,398

The accompanying notes to the basic financial statements are an integral part of this statement.

## COMMONWEALTH OF PUERTO RICO

## MUNICIPALITY OF AÑASCO

Statement of Net Assets (continued)

June 30, 2003

## Liabilities and Net Assets

	<u>Governmental activities</u>
<b>Current liabilities (due within one year):</b>	
Accounts payable	\$ 2,177,741
Accrued liabilities, including accrued interests	161,721
Intergovernmental	1,658,944
Deferred revenues	4,408,410
Current portion of long-term obligations:	
Bonds payable	373,000
Notes payable	106,708
Obligation under capital leases	86,875
Compensated absences	237,723
Claims and judgments	10,000
Total current liabilities	<u>9,221,122</u>
<b>Noncurrent liabilities (due in more than one year):</b>	
Bonds payable	10,556,750
Notes payable, including bond anticipation notes	1,078,868
Compensated absences	1,463,704
Estimated liability for municipal solid waste landfill closure and post closure care costs	<u>3,648,238</u>
Total noncurrent liabilities	<u>16,747,560</u>
Total liabilities	<u>25,968,682</u>
<b>Net assets (liabilities):</b>	
Invested in capital assets, net of related debt	<u>19,463,617</u>
Restricted for:	
Capital projects	2,197,889
Debt service	<u>1,301,166</u>
Total restricted net assets	<u>3,499,055</u>
Unrestricted net liabilities	<u>(11,445,955)</u>
Total net assets	<u>\$ 11,516,717</u>

The accompanying notes to the basic financial statements are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Statement of Activities  
Year ended June 30, 2003

Functions/programs	Expenses	Charges for services	Program Revenues		Net Expenses and Changes in Net Assets
			Operating grants and contributions	Capital grants and contributions	
<b>Governmental activities</b>					
General government	\$ 5,425,376	256,182	-	4,083,678	(\$1,085,516)
Urban and economic development	3,498,512	886,303	166,421	-	(2,445,788)
Public safety	201,874	-	-	-	(201,874)
Health and sanitation	3,363,225	1,423,969	-	-	(1,939,256)
Culture, recreation and education	338,194	-	-	-	(338,194)
Public housing and welfare	937,327	-	260,140	-	(677,187)
Interest on long-term obligations	429,994	-	-	-	(429,994)
<b>Total governmental activities</b>	<b>\$ 14,189,543</b>	<b>2,566,454</b>	<b>426,561</b>	<b>4,083,678</b>	<b>(\$7,117,809)</b>

**General revenues:**

**Taxes:**

Property taxes

\$ 6,589,450

Municipal license taxes

1,419,186

Total taxes

8,008,636

Intergovernmental grants and contribution-unrestricted

1,309,977

Unrestricted investment earnings

99,636

Miscellaneous

350,413

Total general revenues

1,760,026

Net change in net assets

2,650,853

Net assets-beginning of fiscal year, as restated

8,865,864

Net assets-end of fiscal year

\$ 11,516,717

The accompanying notes to the basic financial statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
Balance Sheet - Governmental Funds  
June 30, 2003

	Major funds						Total governmental funds
	General fund	Debt service fund	\$1,850,000 bond issuance fund	State block grant fund	HUD section 108 loan fund	Other governmental funds	
<b>Assets</b>							
Cash	\$937,418	-	-	-	-	-	\$937,418
Receivables, net of allowance for uncollectible accounts:							
Taxes:							
Property taxes	425,703	135,456	-	-	-	-	561,159
Municipal license taxes	73,028	-	-	-	-	-	73,028
Accrued interest	3,701	1,334	-	-	-	-	5,035
Intergovernmental	905,876	-	-	-	-	157,610	1,063,486
Due from other funds	91,748	-	-	-	-	2,478	94,226
Other	354,518	-	-	-	-	-	354,518
Restricted assets:							
Cash with commercial banks including cash equivalents of \$1,021,291	1,021,291	-	-	3,357	2,715,531	657,299	4,397,478
Cash with fiscal agent	-	1,760,304	1,842,144	-	-	38,569	3,641,017
Total assets	<u>3,813,283</u>	<u>1,897,094</u>	<u>1,842,144</u>	<u>3,357</u>	<u>2,715,531</u>	<u>855,956</u>	<u>11,127,365</u>
<b>Liabilities</b>							
Accounts payable	325,832	-	-	-	1,630,599	42,582	1,999,013
Intergovernmental	1,508,173	-	-	-	-	-	1,508,173
Due to other funds	-	4,959	-	-	-	89,267	94,226
Deferred revenues	1,921,313	107,193	-	3,357	1,084,932	475,208	3,592,003
Matured bonds due and payable	-	345,000	-	-	-	-	345,000
Matured interests due and payable	-	143,736	-	-	-	-	143,736
Total liabilities	<u>3,755,318</u>	<u>600,888</u>	<u>-</u>	<u>3,357</u>	<u>2,715,531</u>	<u>607,057</u>	<u>7,682,151</u>
<b>Fund Balances (deficits)</b>							
Reserved for:							
Encumbrances	310,528	-	-	-	-	-	310,528
Debt service	-	1,296,207	-	-	-	-	1,296,207
Capital projects	-	-	1,842,144	-	-	355,745	2,197,887
Unreserved, reported in:							
General fund	(252,562)	-	-	-	-	(106,845)	(359,407)
Total fund balances	<u>57,966</u>	<u>1,296,207</u>	<u>1,842,144</u>	<u>-</u>	<u>-</u>	<u>248,900</u>	<u>3,445,215</u>
Total liabilities and fund balances	<u>\$ 3,813,283</u>	<u>1,897,094</u>	<u>1,842,144</u>	<u>3,357</u>	<u>2,715,531</u>	<u>855,957</u>	<u>\$ 11,127,365</u>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
Statement of Revenues, Expenditures and  
Changes in Fund Balances - Governmental Funds  
Year Ended June 30, 2003

	Major Funds						Total governmental fund
	General fund	Debt service fund	\$1,850,000 bond issuance fund	State block grant fund	HUD section 108 loan fund	Other governmental fund	
<b>Revenues:</b>							
Taxes:							
Property taxes	\$ 5,700,365	811,997	-	-	-	-	\$ 6,512,362
Municipal license taxes	1,346,158	-	-	-	-	-	1,346,158
Charges for services	2,473,339	-	-	-	-	-	2,473,339
Intergovernmental grants and contributions:							
Federal government	-	-	-	953,737	2,915,729	640,773	4,510,239
State government	891,358	-	-	-	-	354,308	1,245,666
Investment earnings	78,355	-	9,978	48	1,840	9,415	99,636
Miscellaneous	350,413	-	-	-	-	-	350,413
<b>Total revenues</b>	<b>10,839,988</b>	<b>811,997</b>	<b>9,978</b>	<b>953,785</b>	<b>2,917,569</b>	<b>1,004,496</b>	<b>16,537,813</b>
<b>Expenditures:</b>							
Current:							
General government	4,768,121	-	7,856	-	299	209,787	4,986,063
Urban and economic development	2,907,577	-	-	-	-	-	2,907,577
Public safety	179,421	-	-	-	-	21,511	200,932
Health and sanitation	2,805,164	-	-	-	-	-	2,805,164
Culture, recreation and education	-	-	-	-	-	101,334	101,334
Public housing and welfare	397,952	-	-	-	-	524,356	922,308
Debt service:							
Principal	303,112	386,750	-	-	-	-	689,862
Interest	64,745	299,697	-	-	-	-	364,442
Capital outlays:							
Construction and remodeling of public facilities	80,108	-	-	953,785	2,917,270	616,846	4,568,009
<b>Total expenditures</b>	<b>11,506,200</b>	<b>686,447</b>	<b>7,856</b>	<b>953,785</b>	<b>2,917,569</b>	<b>1,473,834</b>	<b>17,545,691</b>
Excess (deficiency) of revenues over (under) expenditures	(666,212)	125,550	2,122	-	-	(469,338)	(1,007,878)
<b>Other financing sources (uses):</b>							
Transfers-in from other funds	23,325	111,422	-	-	-	-	134,747
Transfers-out to other funds	(111,422)	-	(9,978)	-	-	(13,347)	(134,747)
Proceeds from issuance of bond anticipation notes	-	-	1,850,000	-	-	361,231	2,211,231
<b>Total other financing sources (uses), net</b>	<b>(88,097)</b>	<b>111,422</b>	<b>1,840,022</b>	<b>-</b>	<b>-</b>	<b>347,884</b>	<b>2,211,231</b>
<b>Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses</b>	<b>(754,309)</b>	<b>236,972</b>	<b>1,842,144</b>	<b>-</b>	<b>-</b>	<b>(121,454)</b>	<b>1,203,353</b>
<b>Fund Balances at beginning of year, as restated</b>	<b>812,274</b>	<b>1,059,234</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>370,354</b>	<b>2,241,862</b>
<b>Fund Balances at end of year</b>	<b>\$ 57,966</b>	<b>1,296,207</b>	<b>1,842,144</b>	<b>-</b>	<b>-</b>	<b>248,900</b>	<b>\$ 3,445,215</b>

The accompanying notes to the basic financial statements are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**

Reconciliation of the Balance Sheet - Governmental Funds  
to the Statement of Net Assets  
June 30, 2003

Governmental activities' amounts reported in the statement of net assets  
and the balance sheet - governmental funds are different because:

Aggregate fund balance reported in the balance sheet - governmental funds	\$ 3,445,215
Add (Deduct):	
Inventories and other current assets are not available to pay current period expenditures, therefore are not reported in the governmental funds	93,253
Capital assets used in governmental activities are not financial resources, therefore are not reported in the governmental funds	24,364,085
Deferred revenues in the governmental funds that are recognized as revenues in the statement of activities	814,192
Debt issued by the Municipality have associated costs that are paid from current available resources in the governmental funds. However, these costs are deferred in the statement of net assets	364,322
The following liabilities are not due (mature) in the current period, therefore are not reported in the governmental funds:	
Accounts payable and accrued liabilities and interest	(196,714)
Intergovernmental payables	(150,771)
Bonds payable and notes	(11,770,326)
Obligation under capital leases	(86,875)
Compensated absences	(1,701,427)
Claims and judgments	(10,000)
Landfill closure and post closure care costs	(3,648,237)
Governmental activities' net assets reported in statement of net assets	\$ 11,516,717

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Statement of Revenues and Expenditures - Budget and Actual  
Budgetary Basis - General Fund  
Year ended June 30, 2003

	Budgeted Amounts		Actual amounts (budgeting basis)	Variance with final budget - over (under)
	Original	Final		
<b>Revenues:</b>				
Property taxes	\$ 917,262	\$ 917,262	\$ 1,201,818	\$ 284,556
Municipal license taxes	1,507,000	1,507,000	1,441,795	(65,205)
Construction excise taxes	200,600	200,600	253,232	52,632
Charges for services	1,030,000	1,030,000	710,726	(319,274)
Intergovernmental grants and contributions	3,975,193	4,841,763	3,810,754	(1,031,009)
Investment earnings	103,000	103,000	74,156	(28,844)
Miscellaneous	2,397,205	2,828,705	2,707,696	(121,009)
Total revenues	<u>10,130,260</u>	<u>11,428,330</u>	<u>10,200,177</u>	<u>(1,228,153)</u>
<b>Expenditures:</b>				
Current:				
General government	5,023,013	5,814,036	5,435,477	378,559
Urban and economic development	3,033,075	3,483,966	3,144,970	338,996
Public safety	194,384	188,384	176,786	11,598
Health and sanitation	639,508	745,664	711,338	34,326
Culture, recreation, and education	313,884	319,884	256,569	63,315
Public housing and welfare	124,928	124,928	115,461	9,467
Debt service:				
Principal	312,401	312,401	303,000	9,401
Interest	218,867	218,867	218,867	-
Capital outlays:				
Machinery, equipment, and vehicles	270,200	220,200	215,436	4,764
Total expenditures	<u>\$ 10,130,260</u>	<u>\$ 11,428,330</u>	<u>\$ 10,577,904</u>	<u>\$ 850,426</u>

**Explanation of Differences:**

**Sources/inflows of financial resources:**

Actual amounts (budgetary basis) "available for appropriations" from the budgetary comparison schedule	\$ 10,200,177
Differences - budget basis to GAAP:	
Net decrease in receivables	(161,936)
Resources considered revenues for budgetary purposes but are not revenues for financial reporting purposes	825,072
Resources considered revenues for financial reporting but not for budgetary purposes	(23,325)

Total revenues as reported on the statement of revenues, expenditures and changes in fund balances - governmental funds \$ 10,839,988

**Uses/outflows of financial resources:**

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	\$ 10,577,904
Differences - budget basis to GAAP:	
Net increase in payables	858,842
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	(111,422)
Outflows of budgetary resources used for financing expenditures that are not expenditures for budgetary purposes	180,876

Total expenditures as reported on the statement of revenues, expenditures and changes in fund balances - governmental funds \$ 11,506,200

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO**

Reconciliation of Statement of Revenues, Expenditures and Changes  
in Fund Balances - Governmental Funds to the Statement of Activities  
Year ended June 30, 2003

Governmental activities' amounts reported in the statement of activities and the statement of Revenues, expenditures and changes in fund balances - governmental funds are different because:

Net change in fund balances reported in statement of revenues, expenditures and changes in fund balances – governmental funds	\$ 1,203,353
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Add (Deduct):

The following revenues recorded in the statement of activities do not provide current financial resources, therefore are deferred in the governmental funds:

Property taxes	77,088
Municipal license taxes	73,028
Charges for services	93,115
Intergovernmental grants and contributions	1,309,977

Governmental funds report capital outlays as expenditures. However in the statement of activities, The cost of those assets is allocated over their estimated useful lives as depreciation and amortization expense. This the amount by which capital outlays exceeded depreciation And amortization expense	3,432,683
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Repayment of principal of long-term obligations is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets	689,862
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Certain interest reported in the statement of activities do not require the use of current financial resources, therefore are not reported as expenditures in the governmental funds.	(65,552)
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Amortization of deferred charges reported in the statement of activities does not require the use of current financial resources, therefore are not reported as expenditures in the governmental funds	(5,185)
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Some expenses reported in the statement of activities do not require the use of current financial resources, therefore are not reported as expenditures in the governmental funds	1,953,426
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Generally, inventory and other current assets are recorded as expenditures in the governmental funds when paid rather than capitalized as an asset. However these assets are capitalized in the statement of net assets. This amount represents the net change in these assets for the year.	12,100
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Proceeds from issuance of bond anticipation notes provide current financial resources to governmental funds, but issuing such debt increases long-term liabilities in the statement of net assets	(2,206,271)
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Net change in net assets reported in statement of activities	<u>\$ 2,650,853</u>
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**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Notes to Basic Financial Statements  
June 30, 2003

**1. Summary of Significant Accounting Policies**

The Municipality of Añasco (the Municipality) is a local municipal government located in Puerto Rico and constituted with full legislative, fiscal and all other governmental powers and responsibilities not expressly assigned to the government of the Commonwealth of Puerto Rico (the Commonwealth).

The Municipality's governmental system consists of executive and legislative branches. The Constitution of the Commonwealth provides for the separation of powers of the executive, legislative and judicial branches. A Mayor elected every four years by the citizens exercises the executive power of the Municipality. The legislative power is exercised by the Municipal Legislature, which is also elected every four years. The General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality, exercises the judiciary power.

The Municipality assumes responsibility for providing services related to public housing, welfare, public safety, health, sanitation, education, culture, recreation, urban and economic development, and many other general and administrative duties.

The accompanying basic financial statements present the financial position and the results of operations of the Municipality as a whole, and its various governmental funds as of and for the year ended June 30, 2003 in conformity with accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (GASB).

**a) *New Financial Reporting Model***

In June 1999, the GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis - for State and Local Governments* (GASB No. 34). This statement establishes new financial reporting requirements for state and local governments. The Municipality adopted the provisions of GASB No. 34 as well as other statements referred to below as of July 1, 2002. These statements require the reporting of new financial information and restructure much of the information that governments have reported in the past. Comparability with financial statements issued in prior years has been affected significantly.

According to the new financial reporting model established by GASB No. 34, the minimum required financial statement presentation applicable to the Municipality is composed of the following elements: (1) Government-Wide Financial Statements (GWFS), (2) Fund Financial Statements, (3) Notes to Basic Financial Statements, and (4) Required Supplementary Information (RSI).

The RSI is a set of reports and information reported along with, but separate from, the Municipality's basic financial statements. In the accompanying basic financial statements, the required RSI is composed of the following elements: (1) Management Discussion and Analysis (MD&A) and, (2) the Schedule of Funding Progress-Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities (ERS).

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Notes to Basic Financial Statements  
June 30, 2003

The MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the year ended June 30, 2003, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

The accompanying Schedule of Funding Progress - Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities provides unaudited three-year trend information (using latest data available) of the funding status of ERS, which is a multi-employer cost-sharing retirement system in which the Municipality is a participating employer.

As previously mentioned, other statements and interpretations were required to be adopted in conjunction with GASB No. 34. Therefore, the Municipality has also adopted the following pronouncements at July 1, 2002: (1) GASB Statement No. 33 - *Accounting and Financial Reporting for Nonexchange Transactions*, (2) GASB Statement No. 37 - *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus*, (3) GASB Statement No. 38 - *Certain Financial Statement Note Disclosures*, and, (4) GASB Interpretation No. 6 - *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

GASB No. 34 also requires that the accounting for all governmental activities reported in the GWFS be based on applicable pronouncements issued by the Financial Accounting Standards Board (FASB) and its predecessor bodies, such as the Accounting Principles Board (APB), issued on or before November 30, 1989, provided those pronouncements do not conflict with or contradict GASB pronouncements. Accordingly, simultaneously with the adoption of GASB No. 34, the Municipality also adopted the following pronouncements: (1) APB Opinion No. 20 - *Accounting Changes*, (2) APB Opinion No. 21 - *Interest on Receivables and Payables*, (3) FASB Statement No. 5 - *Accounting for Contingencies*, and (4) FASB Statement No. 16 - *Prior Period Adjustments*. The Municipality has elected to not apply all Statements and Interpretations issued by FASB after November 30, 1989, in accordance with GASB No. 20.

The effects of implementing the aforementioned pronouncements have been reported as changes in accounting principles in the accompanying basic financial statements. Accordingly, the cumulative effects of the adoption of such pronouncements have been reported as restatements of fund balances/deficits at July 1, 2002 in the accompanying governmental fund financial statements.

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**b) *Financial Reporting Entity***

The accompanying basic financial statements include all departments, agencies and municipal entities that: (1) are under the legal and administrative control of the Mayor, and (2) whose funds are under the legal custody and control of the Municipality's Director of Finance, as prescribed by Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipalities Act of the Commonwealth of Puerto Rico*.

The Municipality's management has considered all potential component units for which it may be financially accountable and other legally separate organizations for which the nature and significance of their relationship with the Municipality may be such that exclusion of their financial statements from those of the Municipality would cause the Municipality's basic financial statements to be misleading or incomplete.

GASB Statement No. 14, - *The Financial Reporting Entity* (GASB No. 14), has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the Municipality to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Municipality.

The Municipality's management has concluded that, based on the aforementioned criteria, there are no legally separate entities or organizations that should be reported as component units of the Municipality as of June 30, 2003 nor for the year then ended.

The GASB recently issued its Statement No. 39, *Determining Whether Certain Organizations are Component Units* (GASB No. 39). This statement is effective for the Municipality's next fiscal year and amended the provisions of GASB No. 14 to provide additional guidance to determine whether certain organizations for which the Municipality is not financially accountable should be reported as component units based on the nature and significance of their relationship with the Municipality. Generally, GASB No. 39 will require reporting, as a discretely presented component unit, an organization that raises and holds economic resources for the direct benefit of a governmental entity. Such organizations are legally separate, tax-exempt entities that meet all of the three specific criteria that address benefit, entitlement or access, and significance. At June 30, 2003, the Municipality has not adopted the provisions of GASB No. 39; however, the Municipality's management has concluded that the future adoption of GASB No. 39 will not have an impact on the Municipality's basic financial statements since no change in the Municipality's financial reporting entity is expected.

**c) *Government-Wide Financial Statements***

The accompanying government-wide financial statements (GWFS) are composed of: (1) the statement of net assets and (2) the statement of activities. These financial statements do not report fund information but rather report information of all of the Municipality's non-fiduciary governmental activities. These statements are aimed at presenting a broad overview of the Municipality's finances through reporting its financial position and results of operations as a whole, using methods that are similar to those used by most private businesses.

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The focus of the GWFS is not on compliance with budgets, regulatory requirements or on the use of available or currently expendable financial resources (referred to as fiscal accountability), but on operational accountability information about the Municipality as a single economic unit. Operational accountability is the Municipality's responsibility to report to the extent to which it has met its operating objectives efficiently and effectively, using all resources available for that purpose. It focuses on the Municipality's principal operating objective, which is to provide services to its citizens.

The accompanying statement of net assets provides short-term and long-term information about the Municipality's financial position and condition by presenting all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity) or "net liabilities" (deficit). This statement assists management in assessing the level of services that can be provided by the Municipality in the future, and its ability to meet its obligations as they become due. In addition, this statement reports the extent to which the Municipality has invested in capital assets, including infrastructure; and discloses legal and contractual restrictions on resources.

Net assets (liabilities) are classified in the accompanying statement of net assets within the following three categories:

- **Invested in Capital Assets, Net of Related Debt** – These consist of capital assets, net of accumulated depreciation and amortization and reduced by the outstanding balances of bonds, notes and any other debt that are attributed to the acquisition, construction, or improvement of those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvement of capital assets have been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs.
- **Restricted Net Assets** – These consist of net assets restricted by external parties (such as creditors, grantors, contributors, laws or regulations of other governments, etc.), or net assets for which constraints are imposed by constitutional provisions or enabling legislation. Enabling legislation is defined as legislation that authorizes the Municipality to assess, levy, charge, or otherwise mandates payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

The classification of restricted net assets is intended to identify resources that have been received or earned by the Municipality with an explicit understanding between the Municipality and the resource providers that the resources would be used for specific purposes. Grants, contributions and donations are often given under those kinds of conditions. Bond indentures also often limit the use of bond proceeds to specific purposes.

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Internally imposed designations of resources, including earmarking, are not reported as restricted net assets. These designations consist of management's plans for the use of resources which are subject to change at the discretion of the Municipal Legislature.

- **Unrestricted Net Assets** – These consist of net assets that are neither externally or legally restricted, nor invested in capital assets. However, unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

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

The accompanying statement of activities presents the results of the Municipality's operations by showing how the Municipality's net assets changed during the year ended June 30, 2003, using the net (expense) revenue format. This statement presents the cost of each function/program as well as the extent to which each of the Municipality's functions, programs, or other services either contributes to or draws from the Municipality's general revenues (such as property taxes, municipal license taxes, construction excise taxes, etc.).

A function/program describes a group of activities that are aimed at accomplishing a major service or regulatory responsibility. The functions/programs reported in the accompanying basic financial statements are: (1) general government, (2) urban and economic development, (3) public safety, (4) health and sanitation, (5) culture, recreation and education, and (6) public housing and welfare. The governmental operations of the Municipality's departments and operational units are classified within the following functions/programs in the accompanying basic financial statements:

**General government:**

- Municipal legislature
- Mayor's office
- Department of finance
- Department of human resources
- Department of municipal secretary
- Department of internal audit
- Department of federal programs
- Department of public relations

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**Urban and Economic Development:**

Department of public works

**Public Safety:**

Department of civil defense

**Health and Sanitation**

Family health center of Añasco

Department of sanitation

**Culture, Recreation and Education:**

Department of recreation and sports

**Welfare:**

Center for the elderly

The statement of activities demonstrates the degree to which direct expenses of a given function/program or segments are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function, segment or operational unit. This statement reports revenues in two broad categories: (1) program revenues and (2) general revenues.

Program revenues are generated directly from a program itself or may come from parties outside the Municipality's taxpayers or citizenry. In the statement of activities, program revenues reduce the cost (expenses) of the function/program to arrive at the net cost of the function/program that must be financed from the Municipality's general revenues. The accompanying statement of activities separately reports the following categories of program revenues:

- **Charges for services** – These generally consist of exchange or exchange-like transactions involving charges to customers or applicants who purchase, use, or directly benefit from the goods, services, or privileges provided, or are otherwise directly affected by the services. These include fees charged for specific services, charges for licenses and permits, and fines and forfeitures, among others.
- **Program-specific capital and operating grants and contributions** – These 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.

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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 and reduce the net expense of that program to the Municipality. They are reported net of estimated uncollectible amounts.

General revenues are the default category for revenues. It includes all revenues and gains that do not meet the definition of program revenues. Property taxes, municipal license taxes and construction excise taxes are reported as general revenues. All other nontax revenues (including unrestricted investment earnings, grants and contributions and special items, among others) that do not meet the definition of program revenues are classified as general revenues. Resources that are dedicated internally by the Municipality are reported as general revenues rather than as program revenues. All general revenues are reported net of estimated uncollectible amounts which are recorded as reduction of revenues rather than as expenses.

The *general government* function/program reported in the accompanying statement of activities, includes expenses that are, in essence, indirect or overhead expenses of the Municipality's other functions/programs. Even though some of these costs have been charged to other funds in the governmental fund financial statements as indirect cost allocations permitted under some federal programs, the Municipality has reported these indirect expenses as direct expenses of the general government function. Accordingly, the Municipality does not allocate general government (indirect) expenses to other functions.

The effects of all interfund governmental activities (revenues, expenditures and other financing sources/uses among funds) have been removed from the accompanying statements of net assets and activities.

The Municipality classifies all of its activities as governmental activities in the accompanying GWFS. These are activities generally financed through taxes, intergovernmental revenues, and other nonexchange revenues that can be used to support the Municipality's programs or services. These governmental activities are also generally reported in the governmental fund financial statements.

The accompanying GWFS do not report fiduciary activities, which are those in which the Municipality would be holding or managing net assets for specific individuals or other external parties in accordance with trust agreements or other custodial arrangements. In addition, the Municipality has no significant operations or activities that are financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public is financed primarily through user charges.

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Accordingly, the accompanying GWFS do not report fiduciary nor business-type activities.

**d) *Governmental Fund Financial Statements***

The accompanying governmental fund financial statements (GFFS) are composed of: (1) the balance sheet – governmental funds and (2) the statement of revenues, expenditures and changes in fund balances – governmental funds. These financial statements report the financial position and results operations of the Municipality's governmental funds by presenting sources, uses, and balances of current financial resources. These financial statements often have a budgetary orientation and focus primarily on: (1) the Municipality's major funds, as defined below, (2) the fiscal accountability, and (3) the individual parts of the Municipality's government. Fiscal accountability represents the Municipality's responsibility to justify that its actions in the current year have complied with public decisions concerning the raising and spending of public moneys in the short term (usually one budgetary cycle or one year).

Each governmental fund is considered an independent fiscal entity accounted for within a set of self-balancing accounts that comprise its assets, liabilities, fund equity or deficit, revenue, and expenditures. The accompanying GFFS segregate governmental funds according to their intended purpose and are used in demonstrating compliance with legal, financial and contractual provisions. The minimum number of governmental funds is maintained consistent with legal and self-imposed managerial requirements established by the Municipality. For financial reporting purposes, the Municipality classifies its governmental funds within the following categories:

- ***General Fund*** – The general fund is the Municipality's chief operating and major fund, as defined below, used to account for all financial resources and governmental activities, except for financial resources required to be accounted for in another fund type. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) GAAP requirements, or (3) the demands of sound financial administration requiring the use of a fund other than the general fund.
- ***Special Revenue Funds*** – The special revenue funds are major and nonmajor funds used by the Municipality to account for revenues derived from grants or other revenue sources (other than major capital projects) that are either self-restricted by the Municipality or legally restricted by outside parties for use in specific purposes. The uses and limitations of each special revenue fund are specified by municipal ordinances or federal and state statutes.

However, resources restricted to expenditure for purposes normally financed from the general fund are reported in the Municipality's general fund provided that all applicable legal requirements are appropriately satisfied. In this case, a special revenue fund to account for such kind of transactions will be used only if legally mandated.

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- **Debt Service Fund**— The debt service fund is a major fund, as defined below, used by the Municipality to account for the accumulation of resources for, and the payment of, principal and interest for: (1) bonds and notes for which debt service payments are legally mandated to be accounted for in a debt service fund, and/or (2) general long-term debt for which the Municipality is being accumulating financial resources in advance, to pay principal and interest payments maturing in future years. General long-term debts for which debt service payments do not involve the advance accumulation of resources (such as capital leases, compensated absences, claims and judgments, notes payable to CRIM and federal government, federal cost disallowances, and solid waste landfill closure and post-closure costs, among others) are accounted for in the general fund. Long-term debt's principal and accrued interests due on July 1 of the following fiscal year are accounted for as fund liabilities in the debt service fund at June 30, if resources are available at June 30 for its payment.
  
- **Capital Projects Funds** – Capital projects funds are nonmajor funds, as defined below, used to account for the financial resources used in the acquisition or construction of major capital facilities, other assets and permanent improvements. Significant capital outlays financed from general obligation bond proceeds are accounted for also in the capital projects funds.

The use of the capital projects funds has been reserved for major capital acquisitions or construction activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as vehicles and other minor capital assets) have been reported in the fund from which financial resources were used for the purchase.

Prior to GASB No. 34, the Municipality was required to report governmental fund financial statements that presented a single aggregated column for each fund type. Each column presented the combined total of all funds of a particular type. Fund types are still reported in certain cases, but they are no longer the focus of the accompanying governmental fund financial statements. Under GASB No. 34, the focus of the governmental fund financial statements is on major funds, which generally represent the Municipality's most important funds. Accordingly, the Municipality is required to segregate governmental funds among major and nonmajor categories within the governmental fund financial statements. Major individual governmental funds are reported as individually as separate columns in the governmental fund financial statements, while data from all nonmajor governmental funds are aggregated into a single column, regardless of fund type.

By definition, the Municipality's general fund is always considered a major governmental fund for financial reporting purposes. In addition, any other fund is considered a major fund for financial reporting purposes if its total assets, liabilities, revenues or expenditures of that

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individual governmental fund are at least 10 percent of the corresponding element total (assets, liabilities, revenues or expenditures) for all governmental funds. For the purposes of applying the aforementioned major fund criteria, no eliminations of interfund balances have been made. Total revenues for these purposes means all revenues, including operating and nonoperating revenues (net of allowances), except for other financing sources. Total expenditures for these purposes means all expenditures, including operating and nonoperating expenditures, except for other financing uses.

As previously discussed, the Municipality has no assets held in a trustee or agency capacity for others, nor has significant operations or activities that are financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public is financed primarily through user charges. As a result, the Municipality does not report fiduciary nor proprietary funds in the accompanying basic financial statements.

*e) Measurement Focus and Basis of Accounting*

**Government-Wide Financial Statements** – The accompanying GWFS are prepared using the economic resources measurement focus and the accrual basis of accounting. Subject to the additional rules and limitations detailed below, revenues (including investment earnings) are generally recorded when earned and expenses are generally recorded when a liability is incurred, regardless of the timing of related cash flows.

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are generally recorded when the exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values. An exchange-like transaction is one in which there is an identifiable exchange and the values exchanged, though related, may not be quite equal. Nevertheless, the exchange characteristics of the exchange-like transaction are strong enough to justify treating it as an exchange for accounting purposes (examples include fees for licenses and permits, charges for services, and miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received).

All revenues, expenses, gains, losses and assets resulting from nonexchange transactions are recorded using the criteria set forth by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions* (GASB No. 33), which the Municipality adopted on July 1, 2002. GASB No. 33 established accounting and reporting standards for nonexchange transactions involving cash and financial or capital resources (for example, most taxes, grants and private donations). In a nonexchange transaction, the Municipality gives (or receives) value without directly receiving (or giving) equal value in return. This is different from an exchange transaction, in which each party receives and gives up essentially equal values. According to GASB No. 33, the Municipality groups its nonexchange transactions into the following four classes in the accompanying basic financial statements: (a) derived tax revenues, (b) imposed nonexchange revenues; (b) government mandated nonexchange transactions; and (c) voluntary nonexchange transactions.

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In the case of derived tax revenue transactions (such as municipal license taxes), which result from assessments the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred (that generally is, when the taxpayers' net sales or revenues subject to tax take place).

In the case of imposed nonexchange revenue transactions (such as property taxes), which result from assessments made by the Municipality on nongovernmental entities, including individuals, other than assessments on exchange transactions, receivables are generally recorded in the period when an enforceable legal claim has arisen. Property taxes are generally recorded as revenues (net of amounts considered not collectible) in the period when resources are required to be used or the first period that the use of the resources is permitted.

Government-mandated nonexchange transactions (such as federal and state grants and contributions) result when a government at one level (such as the federal or state government) provides resources to another government (such as the Municipality), and the provider government requires the recipient government to use those resources for a specific purpose or purposes established in the provider's enabling legislation. In these type of transactions, receivables and revenues are generally recorded when all eligibility requirements imposed by the provider have been met. For the majority of grants, resources must be expended by the Municipality on the specific purpose or project before the provider reimburses any amounts. Revenue is, therefore, generally recognized as qualifying reimbursable expenditures are incurred.

Voluntary nonexchange transactions (such as donations and certain grants and entitlements) result from legislative or contractual agreements, other than exchanges, entered into willingly by two or more parties. In these types of transactions, receivables and revenues are generally accounted for in the same manner as government-mandated nonexchange transactions discussed above.

Receipts of any type of revenue sources collected in advance for use in the following period are recorded as deferred revenues.

Events that are neither exchange nor nonexchange transactions are recorded when it is probable that a loss has been incurred and the amount of loss is reasonably estimable.

The measurement focus and the basis of accounting used in the accompanying GWFS differ significantly from the measurement focus and basis of accounting used in the preparation of the accompanying GFFS. Therefore, the accompanying GFFS include reconciliations with brief explanations to better identify the relationship between the GWFS and the GFFS.

**Governmental Fund Financial Statements** - The accompanying GFFS are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current year or soon enough thereafter to pay liabilities of the current year. For this purpose, the Municipality considers most revenues to be available if collected within 90 days after June 30, 2003, except for property taxes for which the availability period is 60 days.

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Revenue sources not meeting these availability criteria or collected in advance are recorded as deferred revenues at June 30, 2003. The principal revenue sources considered susceptible to accrual include property taxes, municipal license taxes, intergovernmental grants and contributions, and investment earnings. These principal revenue sources meet the measurability and availability criteria in the accompanying GFFS.

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed above, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are also generally recorded when the exchange takes place. Accordingly, fees for licenses and permits, charges for services, and miscellaneous revenues are recorded as revenues when collected because they are generally not measurable until actually received.

All revenues, expenses, gains, losses and assets resulting from nonexchange transactions are recorded using the previously discussed criteria set forth by GASB No. 33, but subject to and limited by the availability criteria discussed above. Accordingly, municipal license tax receivables and revenues are generally recorded when the underlying exchange has occurred. Property tax receivables are also generally recorded in the period when an enforceable legal claim has arisen while property tax revenues (net of amounts considered not collectible) are also generally recorded in the period when resources are required to be used or the first period that the use of the resources is permitted. Receivables and revenues from federal and state grants and contributions, donations and entitlements are also generally recorded when all eligibility requirements imposed by the provider have been met (generally as qualifying reimbursable expenditures are incurred).

Investment earnings are recorded when earned only if collected within 90 days after year-end since they would be considered both measurable and available.

As previously discussed, on July 1, 2002, the Municipality adopted the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements* (GASBI No. 6), which modifies the recognition criteria for certain expenditures and liabilities reported under the modified accrual basis of accounting and clarifies a number of situations in which the Municipality should distinguish between governmental fund liabilities and general long-term liabilities.

Pursuant to the provisions of GASBI No. 6, expenditures and related liabilities are generally recorded in the accompanying governmental fund financial statements in the accounting period in which the liability is incurred, as under the accrual basis of accounting, but only to the extent that they are normally expected to be liquidated with expendable financial resources.

Modifications to the accrual basis of accounting include:

- Employees' accumulated vacation, sick leave and compensatory time (compensated absences) is recorded as expenditure when utilized. The amount of the unpaid compensated absences has been reported only in the GWFS.

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- Principal and interest on bonds and notes payable are recorded when they mature (when payment is due), except for principal and interest due in July 1 of the following fiscal year, which are recorded when resources are available in the debt service funds (generally June 30).
- Obligations under capital leases, solid waste landfill closure and post closure care costs, amounts subject to judgments under litigation and other long-term obligations are recorded only they mature (when the payment is due).
- Accounts payable and accrued liabilities not expected to be liquidated with available financial resources are recorded in the government-wide financial statements but not in the governmental funds.
- Executory purchase orders and contracts are recorded as a reservation of fund balance.

Liabilities outside the bounds of these exceptions or modifications are reported as governmental fund liabilities when incurred (including salaries, professional services, supplies, utilities, etc.) since these liabilities normally are paid in a timely manner and in full from current financial resources.

The measurement focus of the GFFS is on decreases in net financial resources (expenditures) rather than expenses. Most expenditures are measurable and are recorded when the related governmental fund liability is incurred. Allocation of costs, such as depreciation and amortization, are not recognized in the accompanying GFFS.

Under the new financial reporting model established by GASB No. 34, all general capital assets and the unmaturing long-term liabilities (determined using the modified accrual basis of accounting) are no longer reported in account groups within the governmental fund balance sheet but are now incorporated into the GWFS.

*f) Stewardship, Compliance and Accountability*

**Budgetary Control**

According to the Autonomous Municipalities Act of the Commonwealth of Puerto Rico, the Mayor and its Administrative Cabinet prepare each fiscal year an annual budget for the Municipality's general fund and debt service fund. Such legally adopted budget is based on expected expenditures by program and estimated resources by source for both funds. The annual budget is developed using elements of performance-based program budgeting and zero-based budgeting, and includes an estimate of revenues and other resources for the ensuing fiscal year under laws and regulations existing at the time the budget is prepared.

The Mayor must submit an annual budgetary resolution project (the project) to the Commissioner of Municipal Affairs of Puerto Rico (the Commissioner) and the Municipal Legislature no later than each May 10 and May 15, respectively. The Commissioner preliminary verifies that the project complies with all the applicable laws and regulations and may provide comments and suggestions to the Mayor on or before each June 13.

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The Municipal Legislature has 10 business days up to no later than June 13 to discuss and approve the project with modifications. The Municipal Legislature may amend the budget submitted by the Mayor but may not increase any items so far to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. After the Municipal Legislature modifies and preliminarily approves the project, the modified project is sent back to the Mayor for his approval or rejection within 6 days. The Mayor may decrease or eliminate any line item but may not increase or insert any new line item in the budget. The Mayor may also veto the budget in its entirety and return it to the Municipal Legislature with his objections. If the project is rejected by the Mayor, the Municipal Legislature will have up to 8 days to adopt or reject the recommendations or objections of the Mayor. The approved project is sent again to the Mayor, which then would have 3 days to sign and approve it.

If a budget is not adopted prior to the end of the deadlines referred to above, the annual budget for the preceding fiscal year, as approved by the Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until the Municipal Legislature and the Mayor approve a new budget. This permits the Municipality to continue making payments for its operations and other purposes until the new budget is approved.

The annual budget may be updated for any estimate revisions as well as year-end encumbrances and may include any additional information requested by the Municipal Legislature. The Mayor may request subsequent amendments to the approved budget, which is subject to the approval of the Municipal Legislature.

For day to day management control, expenditures plus encumbrances may not exceed budgeted amounts at the expenditure-type level of each cost center (activity within a program within a fund). The Mayor may transfer unencumbered appropriations within programs within funds. Appropriation control is by program within a fund. The Municipal Legislature may transfer amounts among programs within and between funds.

Under the laws and regulations of the Commonwealth, the appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided.

**Budgetary Accounting**

The Municipality's annual budget is prepared under the budgetary basis of accounting, which is not in accordance with GAAP.

Under the budgetary basis of accounting, revenue is generally recognized when cash is received. Short-term and long-term borrowings may be used to finance budgetary excess of expenditures over revenues.

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Under the budgetary basis of accounting, the Municipality uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control. Accordingly, expenditures are generally recorded when the related expenditure is incurred or encumbered. Available appropriations and encumbrances are established to lapse one year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and encumbrances lapse at year-end. Other appropriations, mainly capital projects appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

**g) *Unrestricted and Restricted Deposits***

The Municipality's deposits are composed of cash on hand and demand deposits in commercial banks and the Government Development Bank for Puerto Rico (GDB), a governmental bank and a major component unit of the Commonwealth, who is statutorily designated as fiscal agent of the Municipality.

The Municipality follows the practice of pooling cash. The balance in the pooled cash account is available to meet current operating requirements and any excess is invested in certificates of deposit with original maturities of more than three months.

Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the federal depository insurance generally provided by the Federal Deposits Insurance Corporation (FDIC). All securities pledged as collateral are held in the Municipality's name by agents designated by the Secretary of the Treasury of the Commonwealth.

Restricted cash for major special revenue and capital projects funds, represent the balance of interest and noninterest bearing accounts restricted to finance the operations of federal and state funded programs and the acquisition, construction and improvement of major capital improvements, respectively.

Restricted cash in other governmental funds represents: (1) resources restricted to finance the operations of federal and state funded programs, and (2) resources restricted for the acquisition, construction and improvements of capital improvements.

**h) *Unrestricted and Restricted Accounts Receivable***

In the accompanying GWFS, receivables consist of all revenues earned but not collected at June 30, 2003. Major receivable balances for the governmental activities include municipal license taxes, property taxes and intergovernmental receivables.

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Tax receivables in the general fund represent uncollected property taxes and municipal license taxes. Tax receivables in the debt service fund consist of uncollected property taxes which are restricted for the payment of the Municipality's debt service, as established by law.

Intergovernmental receivables are mainly composed of amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to state and federally funded programs (recorded in the special revenue fund).

These accounts receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience, historical trends, current economic conditions and the periodic aging of accounts receivable.

Activity 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). All other outstanding balances between funds are reported as "due to/from other funds." Advances between funds, as reported in the GFFS, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

***i) Inventories and Other Current Assets***

Inventories and other current assets recorded consist of materials, supplies, food and medicine inventories held for consumption; and prepaid expenses. Generally, inventories are stated at cost using the first-in, first-out method (FIFO) in the GWFS (consumption method). Inventories and prepaid expenses in the GFFS are recorded as expenditures (purchase method) when purchased (paid) rather than capitalized as an asset. Only significant amounts of inventory or prepaid expenses at the end of the year, if any, would be capitalized in the GFFS.

***j) Cash equivalents***

Cash equivalents are composed of certificates of deposit with original maturities of less than three months. Investments are held with commercial banks and are recorded at cost (which approximates fair value).

***k) Deferred Charges***

Deferred charges capitalized in the accompanying statement of net assets consist of bond issuance costs, net of accumulated amortization. Deferred charges are amortized over the term of the related debt using the straight-line method. In the GFFS, bond issuance costs are recognized in the current period as expenditures, whether or not withheld from the actual debt proceeds received.

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***l) Capital Assets***

Capital assets used in governmental activities include land and land improvements, buildings, structures and building improvements, machinery and equipment, furniture and fixtures, licensed vehicles, construction in progress, and infrastructure. These assets are capitalized and reported in the accompanying GWFS. Infrastructure assets are generally immovable in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets. The Municipality has no collection of works of art or historical treasures.

The Municipality defines capital assets as assets with an individual cost of \$500 or more at the date of acquisition or construction, and with a useful lives extending beyond one year. All assets with individual costs under \$500 or with useful lives not exceeding one year, are charged directly to expense in the government-wide statement of activities. In the governmental funds, all capital assets are recorded as expenditures.

In the government-wide statement of net assets, all capital assets are recorded at cost or estimated historical cost if actual cost was unavailable, except for donated capital assets, which are recorded at their estimated fair value at the date of donation. Estimated historical costs based on deflated current costs were used to value a significant portion of the infrastructure and certain land, buildings, structures and building improvements constructed or acquired prior to June 30, 2002. The method to deflate the current costs using an approximate price index was used only in the case of certain items for which their historical cost documentation was not available. Actual historical costs were used to value the infrastructure, land, building, structures, building improvements, construction in progress, machinery and equipment and licensed vehicles constructed or acquired during the year ended June 30, 2003.

Major outlays for capital assets and improvements are capitalized in the GWFS as projects are constructed. The costs of normal maintenance and repairs that do not add value to the asset or materially extend capital asset lives are not capitalized.

Depreciation and amortization expense is recorded only in the government-wide statement of activities. However, there is no depreciation or amortization recorded for land and construction in progress. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight- line method, except for machinery and equipment held under capital leases which is depreciated over the shorter of its estimated useful life or the lease term. The estimated useful lives of major capital asset categories are:

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	<u>Years</u>
Land improvements	20
Buildings, structures and building improvements	50
Infrastructure	20 to 50
Motor vehicles	8
Furniture and fixtures	5 to 20
Machinery and equipment, excluding those held under capital leases	5 to 20

Depreciation and amortization expense on capital assets are recorded as direct expenses of the function/program specifically identified with the asset. Depreciation and amortization of infrastructure is not allocated to various functions/programs but reported as direct expenses of the urban and economic development function.

***m) Deferred Revenues***

The Municipality reports deferred revenue on its GFFS and GWFS. In the GFFS, deferred revenue arises when:

- Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period. As previously discussed, available is defined as due (or past due) at June 30, and collected within 90 days thereafter to pay obligations due at June 30, or;
- Resources are received by the Municipality before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, or when the Municipality has a legal claim to the resources, the liability for deferred revenue is removed and revenue is recognized.

Deferred revenues at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them.

***n) Compensated Absences***

Compensated absences are accounted for under the provisions of Statement No. 16, *Accounting for Compensated Absences*, issued by GASB (GASB No. 16). Compensated absences include paid time off made available to employees in connection with vacation, sick leave and compensatory time. The liability for compensated absences recorded in the government-wide statement of net assets is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2003, and (2) is not contingent on a specific event (such as illness) that is outside the control of the Municipality and the employee. The liability for compensated absences, include salary-related costs, which are directly and incrementally related to the amount of salary paid to the employee (such as employer’s share of Social Security taxes, Medicare taxes, employer contributions to the employees’ retirement systems and others).

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The vacation policy of the Municipality provides for the accumulation of regular vacations at a rate of 2.5 days per month (30 days per year). Employees accumulate sick leave at a rate of 1.5 days per month (18 days per year). Compensatory time is accumulated by employees at a rate of 1.5 times the overtime worked. All vacation and sick leave days accumulated by employees in excess of 60 days and 90 days, respectively, are paid to employees each year if not consumed, as required by law. In the case of compensatory time, the excess of 240 hours is paid to employees each year, if not consumed.

Upon termination of employment, an employee receives compensation for all accumulated unpaid regular vacation leave at the current rate. In the case of sick leave, if the employee terminates his or her employment with the Municipality before reaching 10 years of services, such regular sick leave days is not paid to the employee. After 10 years of services any sick leave balance is paid to the employee. Accumulated vacation time is fully vested to the employees at any time.

The liability for compensated absences is reported in the statement of net assets. A liability for compensated absences is reported in the GFFS only if they have matured, for example, as a result of employee resignations and retirements

***o) Long-term Debt***

The long-term liabilities reported in the GWFS include the Municipality's general obligation and public improvements bonds, long-term notes, obligation under capital leases, compensated absences, and legal claims and judgments.

All long-term debt to be repaid from governmental resources is reported as liabilities in the government-wide statement of net assets, except for principal and interest payment on bonds due in July 1 of the following fiscal year, which is recorded in the GFFS when resources are available in the debt service fund (generally at June 30). In the GFFS, long-term debt is generally not reported as liabilities. The face amount of the debt issued is reported as other financing sources.

In the GWFS debt issuance costs are reported as deferred charges and are amortized under the straight-line method over the life of the debt while in the GFFS are recognized as expenditures as during the current period.

On July 1, 2002, the Municipality adopted the provisions of APB Opinion No. 21, *Interests on Receivables and Payables* (APB No. 21), to account for certain non-interest bearing notes payable to the Puerto Rico Treasury Department. According to APB No. 21, the Municipality has recorded these notes at present value with an imputed interest rate that approximates the rate that would have been used, using the same terms and conditions, if had been negotiated by an independent lender. In the accompanying statement of net assets, this note payable is reported net of the applicable unamortized discount, which is the difference between the present value and the face amount of the note.

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The note discount is amortized over the life of the note using the effective interest method. Amortization of the note discount is recorded as part of interest expense in the statement of activities. In the GFFS, note discounts are recognized as other financing uses during the current period.

*p) Leases*

The Municipality classifies its lease agreements either as operating or capital leases. Capital lease agreements are non-cancelable and involve substance over form, the transfer of substantially all benefits and risks inherent in the ownership of the leased property, while operating leases do not involve such transfer. Accordingly, a capital lease involves the recording of an asset and a related lease liability at the inception of the lease. According to GAAP, the Municipality classifies a lease agreement as a capital lease if at its inception, the lease meets one or more of the following four criteria:

- By the end of the lease term, ownership of the leased property is transferred to the Municipality.
- The lease contains a bargain purchase option.
- The lease term is substantially (75% or more) equal to the estimated useful life of the leased property.
- At the inception of the lease, the present value of the minimum lease payments, with certain adjustments, is 90% or more of the fair value of the leased property.

Although the Municipality is prevented legally from entering into obligations extending beyond the current year budget, most capital lease agreements entered by the Municipality contain fiscal funding clauses or a cancellation clause that makes the continuation of the agreements subject to future appropriations. Leases that meet at least one of the aforementioned four criteria and have fiscal funding or cancellation clauses have been recorded as capital leases in the accompanying GWFS, since the likelihood of invoking the provision is considered to be remote. The lease agreements of the Municipality do not include contingent rental payments or escalation clauses.

In the GWFS, the obligation under capital leases is recorded at the lesser of the estimated fair value of the leased property or the present value of the minimum lease payments, excluding any portion representing executory costs and profit thereon to be paid by the lessor. Subsequently, a portion of each minimum lease payment is allocated to interest expense and the balance is applied to reduce the lease liability using the effective interest method.

In the GFFS, the net present value of the minimum lease payments at the inception of the capital lease is recorded as (1) expenditure and (2) other financing source. Minimum lease payments are recorded as expenditures in the GFFS.

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**q) *Solid Waste Landfill Closure and Postclosure Maintenance Care Costs***

Solid waste landfill closure and postclosure maintenance care costs are accounted for under the provisions of Statement No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Costs*, issued by the Governmental Accounting Standards Board (GASB 18).

According to GASB 18, the estimated liability for solid waste landfill closure and postclosure care costs (including monitoring and maintenance) include an estimate of all costs to be incurred near or after the close of the Municipality's solid waste landfill under the accrual basis of accounting. In the accompanying government-wide statement of net assets, this liability is recognized over the useful life of the landfill, even though such costs will only be incurred, by definition, near or after the close of the landfill. The estimates of closing and postclosing costs are made using current costs (costs that would be incurred if the closing date of the landfill would have been June 30, 2003). The liability is adjusted annually to reflect the effects of inflation, advances in technology, changes in regulations or similar changes.

At the fund level, landfill closure and postclosure care costs are recorded in the accompanying statement of revenues, expenditures and changes in fund balances – governmental funds as expenditures in the accounting period in which the liability is incurred. At June 30, 2003, the Municipality has recorded an estimated liability for solid waste landfill closure and postclosure maintenance care costs amounting to \$3,648,238 in the accompanying government-wide statement of net assets.

**r) *Accounting for Pension Costs***

For the purpose of applying the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers* (GASB No. 27), the Commonwealth of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities (ERS) and System 2000, the two retirement systems in which the employees of the Municipality participate. Accordingly, the Municipality is considered a participant and not a sponsor of these retirement systems since substantially all of the participants in the aforementioned pension trust funds are part of the financial reporting entity of the Commonwealth of Puerto Rico. Accordingly, no portion of the net pension obligation (NPO) related to ERS and System 2000 has been allocated to the Municipality in the accompanying basic financial statements. The basic financial statements of the Commonwealth of Puerto Rico accounts for the total amount of the net pension obligation of ERS and System 2000, including any amount that may be allocated to the Municipality.

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The Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions. In the GFFS the statutory contributions and the related liability are accounted for under the modified accrual basis of accounting while in the GWFS, are recorded under the accrual basis of accounting.

**s) *Risk Management***

The Municipality carries commercial insurance covering casualty, theft, tort claims, and other losses. Insurance policies are negotiated by the Commonwealth's Department of Treasury (the Department of Treasury) on behalf of all of municipalities of Puerto Rico. The Department of Treasury pays the insurance premiums on behalf of the Municipality and then is reimbursed each year through monthly equal payments deducted from the Municipality's gross property tax collections made by the Municipal Revenue Collection Center (known as "CRIM", by its Spanish Acronyms), a governmental entity responsible for billing and collecting property taxes on behalf of all municipalities of Puerto Rico.

The Municipality carries insurance coverage for death and bodily injuries caused by automobile accidents. This insurance is obtained through the Automobile Accidents Compensation Administration (known as "AACA", by its Spanish Acronyms), a component unit of the Commonwealth. This insurance is compulsory for all licensed vehicles used on public roads and highways in Puerto Rico. The annual premium is \$35 per licensed motor vehicle, which is paid directly to AACA.

The Municipality provides workers' compensation insurance coverage to its employees through the State Insurance Fund Corporation, a component unit of the Commonwealth. This insurance covers workers against injuries, disability or death because or work or employment-related accidents, or because of illness suffered as a consequence of their employment. Workers' compensation insurance premiums are also paid through monthly deductions made by CRIM from the Municipality's gross property tax collections.

The Municipality provides unemployment compensation, non-occupational disability, and drivers' insurance coverage to its employees through various insurance programs administered by the Commonwealth's Department of Labor and Human Resources (DOL). These insurance programs cover workers against unemployment and provide supplementary insurance coverage for temporary disability, or death because of work or employment-related accidents or because of illness suffered as a consequence of their employment. Unemployment compensation, non-occupational disability and drivers' insurance premiums are paid directly to DOL on a quarterly basis.

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The Municipality also provides medical insurance coverage to all employees. The current insurance policies have not been canceled or terminated at June 30, 2003. In the past three years, the Municipality has not settled claims that exceeded insurance coverage.

**t) Reservations of Fund Balances**

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

- **Encumbrances** – Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts represent reservations of unexpired appropriations and generally will become liabilities in future periods as the goods or services are received.
- **Capital Projects** – Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
- **Debt Service** – Represent fund balances available to finance future debt service payments.
- **Other Specified Purposes** – Represents resources set aside for use under federal and state grant programs accounted for in special revenue funds.

**u) Interfund Transactions**

Permanent reallocations of resources between the Municipality's funds are classified as interfund transfers. The Municipality has the following types of transactions recorded among funds in the GFFS:

- **Operating Transfers** – Represent legally required transfers that are reported when incurred as “operating transfers-in” by the recipient fund and as “operating transfer-out” by the disbursing fund.
- **Intra-Entity Transactions** – Represent transfers between the funds of the Municipality that are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
- **Advances** – Represent the amounts advanced among the funds of the Municipality, which are not considered to be currently available financial resources.

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v) *Use of Estimates*

The preparation of the accompanying basic financial statements in conformity with GAAP requires management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

**2. Deposits and Investments**

The Municipality maintains its deposits of cash with various commercial banks located in Puerto Rico and GDB. The balances deposited in commercial banks are insured by the Federal Deposit Insurance Corporation ("FDIC") up to a maximum of \$100,000 per depositor.

Under the laws and regulations of the Commonwealth, public funds deposited in commercial banks must be fully collateralized for the amounts deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury's agents in the Municipality's name.

The Municipality's bank balances of deposits with financial institutions are categorized to provide an indication of the level of custodial risk assumed by the Municipality at year-end. Risk categories are described as follows:

- Category 1:** Insured or collateralized with securities held by the Secretary of the Treasury's agents in the Municipality's name.
- Category 2:** Collateralized with securities held by pledging financial institution's trust department or agent in the Municipality's name.
- Category 3:** Uncollateralized (This includes any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the Municipality's name.)

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The carrying amount of deposits with financial institutions at June 30, 2003 consists of the following:

	Major funds						Total
	General fund	HUD Section 108 loan fund	Small block grant fund	\$1,850,000 bond issuance fund	Debt service fund	Other Governmental Funds	
Unrestricted:							
Cash in commercial banks	\$ 937,418	-	-	-	-	-	\$ 937,418
Restricted:							
Cash in commercial banks	1,021,291	2,715,531	3,357	-	-	657,299	4,397,478
Cash in GDB, as fiscal agent	-	-	-	1,842,144	1,760,304	38,569	3,641,017
<b>Total</b>	<b>\$ 1,958,710</b>	<b>2,715,531</b>	<b>3,357</b>	<b>1,842,144</b>	<b>1,760,304</b>	<b>693,695</b>	<b>\$ 8,975,913</b>

The bank balance of deposits with financial institutions at June 30, 2003 consists of the following:

	Carrying Amount	Bank Balance
Deposits in commercial banks	\$ 4,843,285	\$ 5,176,135
Deposits in governmental banks	4,132,628	4,132,628
<b>Total</b>	<b>\$ 8,975,913</b>	<b>\$ 9,308,763</b>
Bank balances of deposits:		
Category 1		\$ 5,176,135
Category 2		-
Category 3		4,132,628
<b>Total bank balances</b>		<b>\$ 9,308,763</b>

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Pursuant to the Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico, the Municipality may invest in obligations of the Commonwealth, obligations of the United States of America, certificates of deposit, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, among other things.

**3. Municipal License Taxes**

The Municipality is authorized by law to impose and collect municipal license taxes on all trade or business activities operated by any natural or legal person within the territorial area of Añasco. This is a self-assessed tax based on the business volume in gross sales. The Municipality establishes the applicable tax rates. At June 30, 2003, the municipal tax rates imposed by the Municipality were 1.50% for financing institutions and 0.50% for any other taxpayers. Any taxpayers that have been granted with partial tax exemptions under any of the incentive tax laws of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60% and 90% under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return every April 15 based on the actual volume of business generated in the preceding calendar year. Taxpayers with a sales volume of \$1 million or more must include audited financial statements with their returns. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration. The first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to pay the tax in full on the filing date of the declaration (generally April 15), a 5% discount is granted automatically on the tax amount due. Any municipal license taxes collected in advance (that is, pertaining to a future period) are recorded as deferred revenues.

**4. Property Taxes**

The Municipality is authorized by law to impose and collect personal and real property taxes. Under the laws and regulations of the Commonwealth, personal property taxes can be imposed to any natural or legal person that at January 1 of each year is engaged in trade or business and is the owner of personal property used in trade or business.

Personal property taxes are self-assessed by taxpayers every year generally using the book value of personal property assets owned by the taxpayer at January 1 and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. The total personal property tax rate in force was 6.08% (of which taxpayers pay 5.88% and 0.20% is reimbursed by the Department of Treasury) at June 30, 2003. Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property deflated at 1957 market prices. The total real property tax rate in force was 8.08% (of which 7.88% is paid by taxpayers and 0.20% is also reimbursed by the Department of Treasury) at June 30, 2003.

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Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value (at 1957 market prices). For such exempt amounts, the Department of Treasury assumes payment of the basic tax (4%) to the Municipality, except for property assessed of less than \$3,500 (at 1957 market prices), for which no payment is made.

CRIM is responsible for the billing and collections of real and personal property taxes on behalf of the Municipality. Prior to the beginning of each fiscal year, CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, CRIM advances funds to the Municipality based on the initial estimated collections. CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby 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 December 31. If CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, an additional property tax receivable is recorded at June 30. However, if advances exceed the amount actually collected by CRIM, an intergovernmental payable is recorded at June 30.

Law No. 83 of August 30, 1991, as amended, provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. Such special tax is levied by the Commonwealth but is collected by CRIM. Collections of this special tax are remitted to the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth.

In addition, 1.25% of the total personal and real property taxes collected by CRIM is restricted for the Municipality's debt service requirements and is retained by GDB for such purposes.

The Additional Lottery System of the Commonwealth (the "Additional Lottery") is an operational unit reported as an enterprise fund of the Commonwealth, which currently operates several betting alternatives to the citizens of Puerto Rico. The Additional Lottery is required every year to distribute a portion of its excess of revenues over expenses as follows:

- i. Thirty five percent (35%) of its net earnings (defined as the excess of revenues over expenses less an amount earmarked for the Fund for Rent and Home Improvement Subsidy Program for the Low-Income Qualifying Elderly) is earmarked to the municipalities of the Commonwealth, of which a maximum of \$26 million, on an annual basis, is distributed to the Municipal Equalization Fund held by CRIM to cover operating expenses and permanent improvements of the municipalities.
- ii. An additional amount not exceeding \$16 million, on an annual basis, is distributed to the Municipal Equalization Fund, provided it is within the 35% corresponding to the municipalities of the Commonwealth. When the accumulated municipal appropriations from the municipalities' Puerto Rico Health Reform are covered up to June 30, 1997, these
- iii. resources will be assigned to the Health Insurance Administration, a component unit of the Commonwealth.

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**5. Interfund Receivables, Payables and Transfers**

The composition of interfund balances at June 30, 2003 and for the year then ended is as follows:

	Due from:						
	Major funds						
	General fund	Debt service fund	\$1,850,000 bond issuance fund	State block grant program	HUD seccion 108 loan fund	Other governmental funds	Total governmental funds
<b>Due/advances to:</b>							
<b>Major funds:</b>							
Debt services fund	\$ 4,959	-	-	-	-	-	\$ 4,959
<b>Nonmajor funds:</b>							
Other governmental fund	89,266	-	-	-	-	-	89,266
<b>Total</b>	<b>\$ 94,225</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>\$ 94,225</b>

	Transfer from:						
	Major funds						
	General fund	Debt service fund	\$1,850,000 bond issuance fund	State block grant program	HUD Seccion 108 loan fund	Other governmental funds	Total governmental funds
<b>Transfer to:</b>							
<b>Major funds:</b>							
General fund	-	\$ 111,422	-	-	-	-	\$ 111,422
<b>Nonmajor funds:</b>							
Other governmental fund	23,325	-	-	-	-	-	23,325
<b>Total</b>	<b>\$ 23,325</b>	<b>111,422</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>\$ 134,747</b>

Interfund receivables and payables represent the pending settlements of the aforementioned transfers, which are considered by management to be fully realizable at June 30, 2003.

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**6. Capital Assets**

Capital assets activity for the year ended June 30, 2003 is as follows:

	Balance at June 30, 2002, as restated	Additions, depreciation, and amortization expense	Balance at June 30, 2003
<b>Cost Basis:</b>			
Capital assets, not subject to depreciation and amortization:			
Land	\$ 3,641,020		\$ 3,641,020
Construction in progress	1,603,149	2,467,340	4,070,489
Total cost basis of capital assets, not subject to depreciation and amortization	5,244,169	2,467,340	7,711,509
Capital assets, subject to depreciation and amortization:			
Land improvements	3,229,404		3,229,404
Buildings, structures, and building improvements	10,806,803	1,631,131	12,437,934
Infrastructure	11,716,527	376,525	12,093,052
Other machinery and equipment	1,276,429		1,276,429
Equipment under capital leases	420,648		420,648
Licensed vehicles under capital leases	113,682		113,682
Licensed vehicles	3,534,656	93,013	3,627,669
Total cost basis of capital assets subject to depreciation and amortization	31,098,149	2,100,669	33,198,818
Total cost of capital assets	36,342,318	4,568,009	40,910,327
<b>Accumulated depreciation and amortization:</b>			
Land improvements	2,135,579	142,417	2,277,996
Buildings, structures, and building improvements	2,194,676	194,781	2,389,457
Infrastructure	6,883,460	292,913	7,176,373
Other machinery and equipment	790,897	94,564	885,461
Equipment under capital leases	140,216	210,324	350,540
Licensed vehicles under capital leases	94,736	18,946	113,682
Licensed vehicles	3,171,352	181,381	3,352,733
Total accumulated depreciation and amortization	15,410,916	1,135,326	16,546,242
Net capital assets	\$ 20,931,402	3,432,683	\$ 24,364,085

Depreciation and amortization expense was charged to functions in the accompanying government-

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Depreciation and amortization expense was charged to functions in the accompanying government-wide statement of activities as follows:

General government	\$ 30,204
Public safety	300
Urban and economic development	596,402
Health and sanitation	257,852
Public housing and welfare	13,708
Culture, recreation, and education	236,860
Total depreciation and amortization expense	\$ 1,135,326

**7 Long-Term Obligations**

The general long-term debt activity for the year ended June 30, 2003 was as follows:

	Balance at June 30, 2002, as restated	Borrowings/ additions	Payments/ deductions	Discount accretion	Balance at June 30, 2003	Due Within One Year
Bonds payables	\$ 9,415,250	1,850,000	(335,500)	-	10,929,750	\$ 373,000
Bond anticipation note	-	282,766	-	-	282,766	-
Notes payable:						
Puerto Rico Treasury						
Department(Social Security)	174,189	-	(60,679)	-	113,510	61,647
Puerto Rico Treasury						
Department(Property Tax						
advances)	56,980	-	(6,828)	-	50,152	7,132
CRIM (LIMS)	351,612	-	(27,347)	-	324,265	29,323
CRIM (Delinquent Acc)	414,881	-	-	-	414,881	6,192
Obligation under capital leases	317,543	-	(230,668)	-	86,875	86,875
Compensated absences	1,500,001	201,427	-	-	1,701,428	237,723
Estimated for landfill closure and postclosure care cost	3,462,950	185,288	-	-	3,648,238	-
Claims and judgments	226,089	10,000	(226,089)	-	10,000	10,000
<b>Total</b>	<b>\$ 15,919,495</b>	<b>2,529,481</b>	<b>(887,111)</b>	<b>-</b>	<b>17,561,865</b>	<b>\$ 811,892</b>

Historically, the general fund has been used to liquidate compensated absences, claims and judgments, obligations under capital leases and any other long-term liabilities other than long-term debt.

**a) Debt Limitation**

The Municipality's Legislature is legally authorized to determine the contracting of debts of the Municipality. Nevertheless, the laws and regulations of the Commonwealth also provide that:

- Direct obligations of the Municipality (evidenced principally by bonds and notes) are backed by the full faith, credit and taxing power of the Municipality; and

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- Direct obligations are not to be issued by the Municipality if the amount of the principal of, and interest on, such bonds and notes (and on all such bonds and notes issued thereafter) which are payable in any fiscal year, together with any amount paid by the Municipality in the preceding fiscal year on account of bonds or notes guaranteed by the Municipality, exceed 10% of the total assessed value of the property located within the Municipality plus the balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service.

In addition, before any new bonds or notes are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement.

**b) Bonds Payable**

The Municipality issues general obligation, special obligation and public improvement bonds that can be used to finance the acquisition and construction of capital assets, as well as, to cover certain operating needs, including the payment to suppliers.

The laws and regulations of the Commonwealth provide that public debt of the Municipality will constitute a first claim on the available revenue of the Municipality. Public debt includes general obligation bonds, public improvement bonds and notes payable. The good faith, credit and taxing power of the Municipality are irrevocably pledged for the prompt payment of the principal and interest of the general obligation bonds, public improvement bonds and notes payable.

The Municipality levies an annual additional special tax of 1.40% of the assessed value of personal and real property. The proceeds of this additional special tax are deposited in a sinking fund established at GDB whereby sufficient funds must be set aside to redeem the bonds in minimum annual or biannual principal and interest payments. The proceeds of this special tax are recorded in the debt service fund.

For financial reporting purposes, the outstanding amounts of bonds represent the total principal to be repaid. Bonds and notes payable are composed as follows at June 30, 2003:

<u>General obligation bonds:</u>	<u>Outstanding Amount</u>
\$660,000 serial 2001 bonds due in annual principal installments ranging from \$10,000 to \$55,000; plus interest due in semiannually installments at interest of rates 5.00% through July, 1, 2014	\$650,000
\$1,850,000 serial 2003 bonds due in annual principal installments ranging from \$30,000 to \$140,000; plus interest due in semiannually installments at variable rates (5.00% at June 30, 2003) through July, 1, 2027	1,850,000
	\$ 2,500,000

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**Special obligation bonds:**

\$565,000 serial 1997 bonds due in annual principal installments of \$5,000 to \$12,875 ; plus interest due in semiannually installments at variable rates (7.50% at June 30, 2003) through July, 1, 2014	483,750
\$1,010,000 serial 1999 bonds due in annual principal installments ranging from \$15,000 to \$90,000; plus interest due in semiannually installments at variable rates (8.00% at June 30, 2003) through July, 1, 2025	980,000
\$4,000,000 serial 2000 bonds due in annual principal installments ranging from \$216,000 to \$223,000; plus interest due in semiannually installments at variable rates notes (at June 30, 2003) through August, 1, 2021	4,000,000
	\$ 5,463,750

**Public improvement bonds:**

\$ 685,000 serial 1991 bonds due in annual principal installments ranging from \$70,000 to \$85,000; plus interest due in semiannual installments at variable rates (6.163% to 6.313 at June 30, 2003 ) through July, 1, 2005	230,000
\$2,150,000 serial 1995 bonds due in annual principal installments ranging from \$145,000 to \$235,000; plus interest due in semiannual installments at variable rates ( 7.106% to 7.706% at June 30, 2003) through July, 1 , 2009	1,310,000
\$420,000 serial 1995 bonds due in annual principal installments ranging from \$30,000 to \$70,000; plus interest due in semiannual installments at variable rates (5.70% to 6.20% at June 30, 2003) through July, 1, 2009	270,000
\$865,000 serial 2000 bonds due in annual principal installments ranging from \$40,000 to 90,000 ; plus interest due in semiannual installments at interest rate of 7.50% through July, 1, 2014	765,000
\$415,000 serial 2001 bonds due in annual principal installments ranging from \$13,000 to \$25,000; plus interest due in semiannual installments at interest rates of 3.25% through July, 1, 2024	391,000
	\$ 2,966,000

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Interest rates on serial bonds subject to variable interest rates are reviewed periodically by Government Development Bank (GDB) and are based on GDB's weighted average rate for its commercial paper program, not to exceed 8%. For financial reporting purposes, the outstanding amounts of bonds represent the total principal to be repaid.

Bonds and notes payable are composed as follows at June 30, 2003:

<b>Year Ending June 30,</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2004	\$ 373,000	541,057	\$ 914,057
2005	620,000	613,872	1,233,872
2006	657,500	581,374	1,238,874
2007	608,000	547,693	1,155,693
2008	633,000	513,530	1,146,530
2009-2013	2,726,500	2,045,767	4,772,267
2014-2018	2,260,750	1,354,158	3,614,908
2019-2023	1,946,000	688,347	2,634,347
2024-2028	1,105,000	172,863	1,277,863
Total	<u>\$ 10,929,750</u>	<u>7,058,661</u>	<u>\$ 17,988,411</u>

At June 30, 2003, accrued interest payable on bonds amounted to \$143,735.

**c) Bond Anticipation Notes**

Advances on bond anticipation notes (BAN, s) with the U.S. Department of Rural Development (USDRD) have been recorded within long-term obligation in the accompanying statement of net assets. During the fiscal year ended June 30, 2003, the proceeds received from BAN, s amounted to \$282,766 which has been recorded as other financing sources in his capital projects fund, and as an increase in the BAN,s liability in the statement of net assets. The proceeds of BAN,s have been used to finance construction projects of the Municipality. The Municipality has the ability, to refinance such BAN,s on a long-term basic with GDB. The agreement with GDB permits that, after all approved advances under the financing agreement with USDRD are received by the municipality, the BAN,s be refinanced on a long-term basic. The agreement with GDB is non cancelable and does not expire within one year after June 30, 2003. The obligations under the agreement are not callable during that period, except for violations of the provisions of the agreement, for which compliance is objectively determinable or measurable. At June 30, 2003, no violation has occurred thereafter prior to the issuance of the accompanying financial statements.

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**d) Notes Payable to Puerto Rico Treasury Department (Social Security)**

On April 1, 2000, the Municipality entered into a financing agreement with the Puerto Rico Treasury Department to pay the debt related to social security tax from 1982 to 1986. The original face amount of the note was \$302,408, which is due in monthly principal installments of \$5,250, at an implicit interest rate of 1.58% through May 2005. Outstanding balance at June 30, 2003 is net of the unamortized discount. The outstanding principal and interest balances of the note payable amounted to \$113,510 and \$1,723, respectively, at June 30, 2003. The principal and interests maturities are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 61,647	\$ 1,353	\$ 63,000
2005	51,863	370	52,233
Total	<u>\$ 113,510</u>	<u>\$ 1,723</u>	<u>\$ 115,233</u>

**e) Notes Payable to Puerto Rico Treasury Department (Property tax advances)**

On October 27, 1994, the Municipality entered into a financing agreement with the Puerto Rico Treasury Department to pay the debt related to the excess of property tax advances over collection made by Puerto Rico Treasury Department. The original face amount of the note was \$137,812, which is due in monthly principal installments of \$765.62, at an implicit interest rate of 4.38% through September 2009. Outstanding balance at June 30, 2003 is net of the unamortized discount. The outstanding principal and interest balances of the note payable amounted to \$50,152 and \$7,268, respectively, at June 30, 2003. The principal and interests maturities are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 7,132	\$ 2,054	\$ 9,187
2005	7,451	1,736	9,187
2006	7,785	1,403	9,187
2007	8,132	1,055	9,187
2008	8,496	692	9,187
2009-2013	<u>11,156</u>	<u>328</u>	<u>11,484</u>
Total	<u>\$ 50,152</u>	<u>\$ 7,268</u>	<u>\$ 57,419</u>

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**f) Notes Payable to CRIM (LIMS)**

On August 2, 2001, the Resolution Num. 3 Serie 2001-2002 was enacted which authorized the Municipality to obtain refinancing LIMS Projects, for a term not exceeding 10 years. The repayment agreement bears an imputed interest of 7% at June 30, 2003. The outstanding principal and accrued interest balances of the note payable to CRIM amounted to \$324,265 and \$105,967, respectively, at June 30, 2003. The principal and interest maturities are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 29,323	21,770	\$ 51,093
2005	31,443	19,650	51,093
2006	33,716	17,377	51,093
2007	36,154	14,939	51,093
2008	38,767	12,326	51,093
2009-2013	<u>154,862</u>	<u>19,705</u>	<u>174,567</u>
Total	<u>\$ 324,265</u>	<u>\$ 105,767</u>	<u>\$ 430,632</u>

**g) Payable to CRIM (Delinquent accounts)**

On March 26, 2000, the Resolution Num. 10 Serie 2001-2002 was enacted which authorized the Municipality to obtain up to \$414,881, for a term not exceeding 30 years, for the repayment of bonds issued for the sale of delinquent accounts. The repayment agreement bears interest at variable rates (beginning in 6.50% at June 30, 2003). The outstanding principal and accrued interest balances of the note payable to CRIM amounted to \$414,881 and \$381,079, respectively, at June 30, 2003. The principal and interest maturities are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 6,192	20,340	\$ 26,532
2005	6,504	20,027	26,532
2006	6,832	19,699	26,532
2007	7,178	16,354	26,532
2008	7,540	18,992	26,532
2009-2013	43,812	88,848	132,660
2014-2018	56,048	75,612	132,660
2019-2023	71,702	60,958	132,660
2024-2028	91,726	40,933	132,660
2029-2033	<u>117,344</u>	<u>15,316</u>	<u>132,660</u>
Total	<u>\$ 414,881</u>	<u>\$381,079</u>	<u>\$ 795,960</u>

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***h) Lease Obligations***

The Municipality is obligated under capital leases with third parties that expire through 2008 for the acquisition of equipment. At June 30, 2003, the capitalized costs and the related accumulated amortization of the leased equipment amounted to \$420,648 and \$350,540, respectively, which are accounted for in the accompanying government-wide statement of net assets within capital assets. The present value of the future minimum capital lease payments at June 30, 2003 reported in the accompanying government-wide statement of net assets is as follows:

<u>Year ending June, 30</u>	<u>Amount</u>
2003	\$ 88,164
Total future minimum lease payments	88,164
Less: amount representing future interest cost at 6.00%	1,289
Present value of minimum lease payments	86,875
Less:	
Current portion of obligation under capital leases	86,875
Obligation under capital leases, excluding current portion	<u>\$ 0</u>

***i) Compensated Absences***

At June 30, 2003, the composition of the liability for compensated absences is composed as follows:

	<u>Due Within</u> <u>One Year</u>	<u>Due After</u> <u>One Year</u>	<u>Total</u>
Vacation and sick leave	\$ 118,622	\$1,463,704	\$ 1,582,326
Compensatory time	119,101	-	119,101
Total	<u>\$ 237,723</u>	<u>\$1,463,704</u>	<u>\$ 1,701,427</u>

***j) Landfill Closure and Postclosure Costs***

On July 1, 2002, the Municipality adopted the provisions of Statement No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Costs issued by the Governmental Accounting Standard Board*. This statement established standards for accounting and reporting for solid waste landfill costs owned by governmental entities (including the Municipality) that are required by federal and local laws or regulations to incur closure and postclosure care costs.

According to this statement, closure and postclosure care costs are recorded while the landfill is operating. The Municipality has determined that the present value of total estimated

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closing costs and post closing maintenance care costs amount to \$1,634,519 and \$2,013,720, respectively, as of June 30, 2003.

Of these estimated costs, the Municipality has recorded a liability amounting to \$3,648,238, which is the amount required by GAAP for accrual as of June 30, 2003. The liability was recorded in the accompanying government-wide financial statements with: (1) a charge to health and sanitation expenses for \$185,288, and (2) a restatement (charge) to beginning net assets for \$3,462,950 as a prior-period adjustment related to the portion of the accrual corresponding to prior years that was not recorded as of June 30, 2002 in the general long-term debt account group. Management is of the opinion that the estimated remaining useful life of the landfill is approximately seven years from June 30, 2003.

## **8. Employees' Retirement Systems**

### ***a) Plan Description***

The Municipality's employees participate in the Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities ("ERS"). The ERS is the administrator of a multi-employer (as related to the Municipality's reporting entity) defined pension plan (the "System") established by the Commonwealth. The System was created under Act. No. 447 (the "Act"), approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentalities, the Municipality and other municipalities of the Commonwealth of Puerto Rico.

The System is independent, thus assets may not be transferred to another system or used for any other purpose other than for benefit each system's participants. The System issues publicly available financial reports that include basic financial statements and required supplementary information for each of them, including required six-year trend information. Those reports may be obtained by writing to the administrator of the System.

The System provides for retirement, death and disability benefits. Death and disability retirement benefits are available to members for occupational and non-occupational death and disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after 10 years of plan participation.

Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the System, was enacted with the purpose of establishing a new pension program ("System 2000").

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System 2000 became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999, had the option to either stay in the defined benefit plan or transfer to the new program. Persons employed on or after January 1, 2000, are only allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as cash balance plan. Under this new plan, there is a pool of pension assets, which are invested by the System, together with those of the current defined benefit plan.

Benefits at retirement are not guaranteed by the Commonwealth of Puerto Rico or the Municipality. The annuity is based on a formula which assumes that each year the employees' contribution (with a minimum of 8.275 percent of the participant's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note; (2) earn a rate equal to 75% of the return of ERS's investment portfolio (net of management fees); or (3) earn a combination of both alternatives.

Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employer's contributions (9.275% of the participant's salary) will be used to fund the current plan.

System 2000 reduced the retirement age from 65 years to 60 for those employees who joined the current plan on or after January 1, 2000.

On August 12, 2000, Act No. 174 was approved to allow certain participants of ERS to be eligible for early retirement upon attaining at least age 55 with 25 years of service, provided they made their election on or before April 1, 2001. Those who elected early retirement under this law will receive monthly benefits of 75% (if 25 or more years of service and age 55, or 30 or more years of service and age 50) or benefits of 65% (if 25 years of service by less than age 55) of their average compensation which is computed based on the highest 36 months of compensation recognized by ERS. In the cases, the sponsor contribution with respect to the participants covered until the participants reach the normal retirement age.

Historically, the Commonwealth of Puerto Rico has reported ERS and System 2000 in its basic financial statements. Accordingly, the Commonwealth of Puerto Rico is currently assuming any actuarial deficiency that may exist or arise related to the Municipality's participating employees since the System does not allocate any actuarial deficiencies pertaining to municipal employees participating in the System. The Municipality is only required by law to make statutory contributions in the rates detailed below.

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**b) Funding Policy**

Contribution requirements are established by law and are as follows:

Municipality and other employers      9.275% of applicable payroll

Employees:

Hired on or before March 31, 1990    5.775% of monthly gross salary up to \$550

8.275% of monthly gross salary up to \$550

Hired on or before April 1, 1990      8.275% of monthly gross salary

**c) Annual Pension Cost and Net Pension Obligation**

The net pension obligation and the annual pension cost of ERS and System 2000 as of and for the year ended June 30, 2002 (most recent data available), which include the employees of the Municipality, the Commonwealth of Puerto Rico and other municipalities, has been recorded in the basic financial statements of the Commonwealth. No allocation of such amounts has been made in the accompanying basic financial statements. The following aggregate annual pension cost and net pension obligation as of and for the year ended June 30, 2002 (most recent data available) which are assumed and accounted for by the Commonwealth, is presented only for the purposes of additional analysis (amounts expressed in thousands):

Annual required contributions	\$ 802,536
Interest on net pension obligation	192,416
Adjustment to annual required employers' contributions	<u>(134,870)</u>
Annual pension cost	860,082
Statutory employers' contributions made	<u>(308,228)</u>
Increase (decrease) in net pension obligation	551,854
Net pension obligation at beginning of year	<u>2,263,722</u>
Net pension obligation at end of year	<u>\$ 2,815,576</u>

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The annual required contribution recorded at June 30, 2002 (most recent data available) in the basic financial statements of the Commonwealth was determined by actuarial valuations for the pension plans as described below:

Date of latest actuarial valuation:	July 1, 2001
Actuarial cost method:	Projected unit credit cost
Amortization cost method:	Level percentage of projected payroll
Remaining amortization period:	25 years
Amortization approach:	Closed
Asset valuation method:	Market Value
Actuarial assumptions:	
Inflation	3.50%
Investment rate of return	8.50%
Projected salary increases per annum	5.00%
Cost-of-living adjustments	3.0% every three years

**d) Three-Year Trend Information**

The three-year trend information is as follows (most recent data available; expressed in thousands):

<b>Annual pension cost (APC):</b>	
Year ended June 30, 2002	\$ 860,082
Year ended June 30, 2001	803,526
Year ended June 30, 2000	768,761

<b>Percentage of APC contributed:</b>	
Year ended June 30, 2002	35.8%
Year ended June 30, 2001	65.6%
Year ended June 30, 2000	35.8%

<b>Net pension obligation:</b>	
Year ended June 30, 2002	\$ 2,815,576
Year ended June 30, 2001	2,263,722
Year ended June 30, 2000	2,010,051

**9. Commitments and Contingencies**

**a) Commitments**

As of June 30, 2003, the Municipality has several outstanding or planned non-cancelable construction projects amounting to \$8,683,574, of which \$4,070,489 have been incurred and

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paid as of June 30, 2003, and \$4,613,085 remain outstanding to incur through the end of each project. These projects are evidenced by contractual commitments with contractors and are accounted for in the capital projects fund.

The Municipality has reported in the general fund, outstanding encumbrances amounting to \$310,528 which the Municipality intends to honor and will continue to be liquidated under the current year's budget during a lapse period that extends into the subsequent fiscal year.

**b) Contingencies**

The Municipality is defendant in numerous claims and legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1995, as amended, persons are authorized to sue the Municipality only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Municipality may provide its officers and employees with legal representation, as well as assume the payment for any judgment that may be entered against them. There is no limitation on the payment of such judgments. With respect to pending and threatened litigation, the Municipality has reported liabilities amounting to \$10,000 for awarded and anticipated unfavorable judgments at June 30, 2003. This amount was included as a long-term obligation in the accompanying statement of net assets, and represents the amount estimated as a probable liability or a liability with a fixed or expected due date, when will require future available financial resources for its payment. Management believes that the ultimate liability in excess of amounts recorded in the accompanying statement of net assets, if any, would not be material to the basic financial statements taken as a whole.

The Municipality receives financial assistance from the federal government in the form of grants and entitlements. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal laws and regulations, including the expenditure of resources for eligible purposes. Accordingly, expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantor. Disallowance as a result of these audits may become liabilities of the Municipality. The "*Reports on Compliance and Internal Control in Accordance with Government Auditing Standards and the Requirements of OMB Circular A-133*" for the year ended June 30, 2003, disclosed various instances of noncompliance with applicable laws and regulations and with internal accounting and administrative controls. If expenditures are disallowed due to noncompliance with grant programs regulations, the Municipality may be required to reimburse the grantor. Management believes that the Municipality will be able to comply with the terms of corrective action plans that may be requested by the federal grantors, consequently, the accompanying basic financial statements do not include any provision or reserve for possible disallowed costs arising from the federal funds disbursed during fiscal year ended June 2003.

On December 2000, the municipality and other municipalities of Puerto Rico filed a complaint against the Puerto Rico Electric Power Authority (PREPA), a component unit of

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the Commonwealth, in the San Juan Court requesting the payments by PREPA of the full contribution in lieu of taxes and electric sales set side for prior fiscal year. The complaint challenged the application by PREPA of the "net revenues" formula which reduced the amount available to pay contributions in lieu of taxes and energy sales set aside for the Municipality. On March 18, 2003, the Board of Directors of PREPA approved a resolution by which PREPA agree to settle the claims with all municipalities. Accordingly, PREPA offered to pay \$125 million to all municipalities to settle the claim, which are divided in \$68 million in cash and \$57 million in the construction of electric infrastructure projects on behalf of the municipalities. Of such amounts, the municipality would \$485,611 in cash and \$407,056 in construction projects. However, at June 30, 2003, the municipality's Legislature and Managements have not accepted the offer from PREPA, and accordingly no receivable or revenue for these concepts has been recorded in the accompanying basic financial statements.

**10. Accounting Changes, Changes in Reporting Entity and Restatements**

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

GASB No. 38 requires certain note disclosures when GASB No. 34 is implemented. The provisions of this new standard have been incorporated into the basic financial statements and notes.

GASB Interpretation No. 6 clarifies the application of existing standards for distinguishing the respective portions of certain types of liabilities that should be reported as (1) governmental fund liabilities and (2) general long-term liabilities of the Municipality. The provisions of this interpretation have been incorporated into the basic financial statements and notes.

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June 30, 2003

These new standards caused most of the accounting changes, changes in reporting entity, and restatements described on the ensuing discussion below. Changes and restatements for reasons other than the adoption of the above pronouncements are also explained below. The following schedule reconciles the June 30, 2002 fund balance as previously reported by the Municipality to the beginning fund balance, as restated:

	June 30, 2002 Fund balance as previously reported in F/S	Fund reclassifications	Reclassifications and adjustments	June 30, 2002 Fund balance as restated
<b>Major funds:</b>				
General fund	\$ 1,053,252	(784,534)	543,556	\$ 812,273
Capital Project :				
SBGP- capital		200,107	(200,107)	-
Industrial Park -section 108		4,000,661	(4,000,661)	-
Debt service fund	1,418,853	-	(359,619)	1,059,234
	<u>2,472,105</u>	<u>3,416,233</u>	<u>(4,016,830)</u>	<u>1,871,508</u>
<b>Other governmental funds:</b>				
Capital projects fund	(673,117)	1,374,851	(283,375)	418,360
Enterprise Fund	(954,214)	954,214	-	-
Special revenue fund	3,702,055	(3,560,696)	(189,364)	(48,005)
Subtotal	<u>2,074,724</u>	<u>(1,231,631)</u>	<u>(472,739)</u>	<u>370,354</u>
Total governmental funds	<u>\$ 4,546,829</u>	<u>2,184,602</u>	<u>(4,489,569)</u>	<u>\$ 2,241,862</u>

Upon the adoption of GASB No. 34, the Municipality revised the classifications of its governmental funds, which resulted in the above presented reclassifications of two nonmajor governmental funds in accordance with GAAP. These governmental fund reclassifications consist of the following:

- The state salary incentives fund, a nonmajor fund reported in previous years as part of the general fund, was reclassified as part of the nonmajor special revenue funds.
- The Añasco economic development fund, a nonmajor fund reported in previous years as a nonexpendable trust fund, was reclassified as part of the nonmajor permanent fund, as required by GASB No. 34.

Upon the adoption of GASB No. 34, the Municipality corrected certain reclassification and adjustments reported in the prior year's governmental funds. These reclassifications and adjustments consist principally in the effect of not adopting the provisions of GASB No. 33 prior to June 30, 2002, as required by GAAP. The reclassification and adjustments in the general fund include the correction of an understatement in cash balances of the general fund.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF AÑASCO**  
Notes to Basic Financial Statements  
June 30, 2003

As part of the implementation of GASB No. 34, the Municipality revised the classifications of its funds for financial reporting purposes. Accordingly, on July 1, 2002, the Municipality reclassified from the enterprise fund to the general fund, the operations of its public medical facilities (known as Añasco Family Health Center). The reclassification was made due to the accumulated deficit of \$954,214 and the net loss of \$619,042 reported by such fund as of and for the year ended June 30, 2003, respectively. Management of the Municipality has concluded that the fees charged by the medical facilities for medical services provided will not be sufficient to recover the cost of providing such services (including capital costs such as depreciation and amortization). The effect of such reclassification, amounting to \$954,214, has been charged to fund balance and accumulated deficit of the general fund and the enterprise fund, respectively. Accordingly, no enterprise fund has been reported in the accompanying fund financial statements.

Correction of errors in the long-term liabilities reported in the prior year's general long-term debt account group are mainly due to record unrecorded amounts and to correct omissions in the respective liability accounts according to GAAP at June 30, 2002.

**REQUIRED  
SUPPLEMENTARY INFORMATION**

**COMMONWEALTH OF PUERTO RICO**

**MUNICIPALITY OF AÑASCO**

Schedule of Funding Progress

Employee' Retirement System of the Government of Puerto Rico and Its Instrumentalities

June 30, 2003

The funding progress of the Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities, based on latest available data, is as follows:

<u>Actual valuation date</u>	<u>Actuarial value of assets</u>	<u>Actuarial accrued liability (AAL)</u>	<u>Unfunded AAL (UAAL)</u>	<u>Funded ratio</u>	<u>Covered payroll</u>	<u>UAAL AS A percentage of covered payroll</u>
July 1, 2001	\$2,429,000	9,881,000	7,452,000	25%	\$2,549,000	292%
July 1, 2000	2,041,800	9,459,300	7,417,500	25%	2,463,400	301%
July 1, 1999	1,858,000	8,308,000	6,450,000	25%	2,275,000	284%

Source: Audited Basic Financial Statements of the Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities (ERS) as of and for the year ended June 30, 2002. At the issuance date of this report, the audited basic financial statements of ERS as of and for the year ended June 30, 2003 has not been issued.

**MUNICIPALITY OF AÑASCO  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2003**

<u>Federal Grantor / Pass-Through Grantor / Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures</u>
<b><u>U.S. DEPARTMENT OF HUD</u></b>		
Direct programs:		
Section 8 Housing Voucher Program	14.177	\$ 351,287
Pass-through Office of the Commissioner of Municipal Affairs:		
Community Development State Block Grant Program (SBGP):		<u>953,785</u>
Total U.S. Department of HUD		<u>1,305,072</u>
<b><u>U.S. DEPARTMENT OF AGRICULTURE</u></b>		
Pass-through the Governor's Office of Child Services and Community Development:		
Child and Adult Care Food Program	10.558	<u>90,197</u>
Total U.S. Department of Agriculture		<u>90,197</u>
<b><u>OTHER FEDERAL ASSISTANCES</u></b>		<u>118,136</u>
Total Federal Assistance		<u>\$1,513,405</u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
NOTES TO SCHEDULE OF EXPENDITURES  
OF FEDERAL AWARDS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**1. GENERAL**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Añasco, Puerto Rico, and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in, or used in the preparation of, the basic financial statements. The Municipality's reporting entity is defined in Note 1-b of the notes to basic financial statements. Federal agencies as well as federal financial assistance passed through other government agencies are included on the schedule.

**2. BASIS OF ACCOUNTING**

- A. The accompanying Schedule of Federal Financial Assistance is presented using the modified accrual basis of accounting, which is described in Note 1-e to the basic financial statements.
- B. The accompanying Schedule of Expenditures of Federal Awards is prepared from the Municipality's accounting records and is not intended to present financial position or the results of operations.
- C. The financial transactions are recorded by the Municipality in accordance with the terms and conditions of the grants, which are consistent with generally accepted accounting principles.
- D. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable or when actually paid, whichever occurs first.

**3. FEDERAL CFDA NUMBER**

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
NOTES TO SCHEDULE OF EXPENDITURES  
OF FEDERAL AWARDS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**4. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS**

Expenditures of federal assistance awards are reported in the Municipality's basic financial statements in the accompanying Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds as Follows:

Expenditures as per basic financial statements:

	<u>Expenditures</u>
State Block Grant Program	\$ 953,785
Other Governmental Fund	<u>559,620</u>
Total expenditures per schedule of expenditures of federal awards	<u>\$1,513,405</u>

*Kenneth Vargas*

**CERTIFIED PUBLIC ACCOUNTANT**

103 LIGHTHOUSE DRIVE RAMEY, P.R. 00603  
Tel./Fax (787) 890-3797

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

The Honorable Mayor, Members of the  
Municipal Legislature and People of  
the Municipality of Añasco  
Añasco, Puerto Rico

I have audited the general purpose financial statements of the Municipality of Añasco, Puerto Rico, as of and for the fiscal year ended June 30, 2003, and have issued my report thereon dated January 26, 2004. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

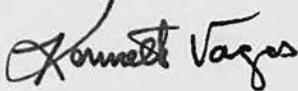
**Compliance**

As part of obtaining reasonable assurance about whether the Municipality of Añasco, Puerto Rico, basic financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit, accordingly, I do not express such an opinion. The results of my tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards* which are described in the accompanying Schedule of Findings and Questioned Costs.

### **Internal Control Over Financial Reporting**

In planning and performing my audit, I considered the Municipality's internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over financial reporting and its operation that I consider to be material weaknesses. However, I noted other matters involving the internal control over financial reporting that I have reported to management of the Municipality of Añasco, Puerto Rico, in a separate letter dated January 26, 2004.

This report is intended solely for the information and use of management, Municipal Council, Office of the Commissioner of Municipal Affairs, and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.



KENNETH VARGAS, CPA  
License 2251

Aguadilla, Puerto Rico  
January 26, 2004

Stamp number 1688096 of the  
Puerto Rico Society of  
Certified Public Accountants  
has been affixed to the  
original copy of this report

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

The Honorable Mayor, Members of the  
Municipal Legislature and People of  
the Municipality of Añasco  
Añasco, Puerto Rico

**Compliance**

I have audited the compliance of the Municipality of Añasco, 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 fiscal year ended June 30, 2003. The Municipality'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 the Municipality's Management. My responsibility is to express an opinion the Municipality's compliance based on my audit.

I conducted my audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of 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 the Municipality's compliance with those requirements and performing such other procedures as I considered necessary in the circumstances. I believe that my audit provides a reasonable basis for my opinion. My audit does not provide a legal determination on the Municipality's compliance with those requirements.

In my opinion, the Municipality of Añasco complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the fiscal year ended June 30, 2003. However, the results of my auditing procedures disclosed instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs.

#### **Internal Control Over Compliance**

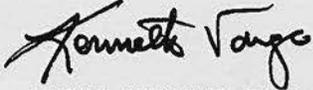
The management of the Municipality of Añasco, Puerto Rico, is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing my audit, I considered the Municipality's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

I noted certain matters involving the internal control over compliance and its operation that I considered to be reportable conditions. Reportable conditions involve matters coming to my attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in my judgment, could adversely affect the Municipality's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, I believe that none of the reportable conditions described above is a material weakness.

Page 3

This report is intended solely for the information and use of management, Municipal Council, Office of the Commissioner of Municipal Affairs, and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.



KENNETH VARGAS, CPA  
License 2251

Aguadilla, Puerto Rico  
January 26, 2004

Stamp number 1688097 of the  
Puerto Rico Society of  
Certified Public Accountants  
has been affixed to the  
original copy of this report

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
SUMMARY OF AUDITOR'S RESULTS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**Financial Statements**

Type of auditor's report issued

**Unqualified**

Internal control over financial reporting:

Material weakness(es) identified?

Yes  No

Reportable condition(s) identified that are not considered being material weaknesses?

Yes  Non Reported

Noncompliance material to financial statements noted?

Yes  No

**Federal Awards**

Internal control over major programs:

Material weakness(es) identified?

Yes  No

Reportable condition(s) identified that are not considered being material weaknesses?

Yes  Non Reported

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?

Yes  No

Identification of Major Programs:

CFDA Number

Name of Federal Program or Cluster

14.219

State Block Grant Program

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

\$300,000

Auditee qualified as low-risk auditee?

Yes  No

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**QUESTIONED  
COSTS**

**Program**

**Federal Assistance Programs**

**FINDING NUMBER 1**

During the examination of the personnel records of the federal programs office personnel, it was observed that in some cases, certain important documentation such as medical certificates, certificates of birth, proof of academic background were missing.

\$-0-

**Recommendation**

The personnel department should review all employee files in order to ascertain that they include the following documents:

- A. Employment application
- B. Medical certification
- C. Certificate of birth
- D. Sworn fidelity
- E. Proof of academic background
- F. Record of promotions and reclassifications
- G. Form 499-R-4 (income tax withholding statement)
- H. Form I-9; "Employment Eligibility Verification Form".  
This form is required by the Immigration Reform and Control Act of 1986. Under this act employers are required to verify identity and eligibility for employment to all persons hired for employment after November 6, 1987.
- I. Certification which makes known that the person does not receive any payment of compensation for services rendered to the State Government or other Municipality. This certification should include a statement which makes clear that the person is not on paid vacations from the State Government or any Municipal Government and to be true, that it be permitted by law.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**QUESTIONED  
COSTS**

- J. Certificate of good behavior
- K. Contract (if applicable)

**Response**

The Personnel Director is in the process of updating all personnel records in order to have them with all the documents or information needed.

**Program**

**State Block Grant Program**

**FINDING NUMBER 2**

The Municipality did not submit the program income report required by the grant agreement.

-0-

**Recommendation**

The municipality should implement proper controls regarding program income.

**Response**

The Federal Program Director has been advised of the finding. Proper controls regarding program income will be implemented in order to assure that the program income reports are submitted on a timely basis.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

**QUESTIONED  
COSTS**

**Program**

**State Block Grant Program**

**FINDING NUMBER 3**

**Cash management**

The office of Federal Funds did not comply with the requirement of maintaining a cash management system with procedures to minimize the time elapsed between the transfer of funds from federal agencies and the disbursements of funds. Various fund requisitions were disbursed over three days from the date the funds were received.

-0-

**Recommendation**

The Municipality should implement a cash management system in order to have better control and minimize the time elapsed between the transfer of funds from federal agencies and the disbursements of the funds. According to program requirements funds should be disbursed not later than three days after they have been received.

**Response**

The mayor gave instructions to the Federal Program Director to establish a cash management system as required by federal program guidelines.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF AÑASCO  
STATUS OF PRIOR YEAR FINDINGS  
AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2003**

During the current engagement of the single audit, the status of prior year findings and question costs were reviewed.

The review disclosed that the conditions still existed and/or no correction action has been taken on the finding Number 1 finding Number 2 and finding Number 3 of this report. These were included in the prior year audit report. Prior year finding number 4 was corrected.