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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO
BASIC FINANCIAL STATEMENTS
WITH ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT
YEAR ENDED JUNE 30, 2009

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

BASIC FINANCIAL STATEMENTS
WITH ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT

YEAR ENDED JUNE 30, 2009

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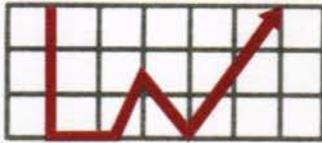
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MUNICIPALITY OF ARECIBO

BASIC FINANCIAL STATEMENTS
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YEAR ENDED JUNE 30, 2009

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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

INDEPENDENT AUDITORS' REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Arecibo
Arecibo, Puerto Rico**

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Arecibo, Puerto Rico**, as of and for the year ended June 30, 2009, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

The financial statements referred to above include only the primary government of the **Municipality of Arecibo**. The financial statements do not include financial data for the legally separated discrete component unit, "Corporación Desarrollo Cultural Teatro Oliver C.E.", which accounting principles generally accepted in the United States of America require to be reported with the financial data of the primary government. As result the primary government financial statements do not purport to, and do not, present fairly the financial position of the reporting entity of the **Municipality of Arecibo**, Puerto Rico, as of June 30, 2009 and the changes in its financial position and its cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

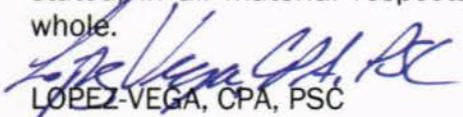
INDEPENDENT AUDITORS' REPORT (CONTINUED)

In our opinion, based on our audit the financial statements referred to above presents fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information for the primary government of the **Municipality of Arcibo, Puerto Rico**, as of June 30, 2009, 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 accordance with Government Auditing Standards, we have also issued our report dated December 29, 2009, on our consideration of the **Municipality's** internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages **3** through **12** and the Budgetary Comparison Schedule-General Fund on page **45** are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We 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, we did not audit the information and express no opinion on it.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 29, 2009

Stamp No. 2407029 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



Certified Public Accountants / Management Advisors

López-Vega, CPA, PSC

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2009

This discussion and analysis of the **Municipality of Arecibo** (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2009. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2008. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

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

FINANCIAL HIGHLIGHTS

The following comments about the financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2009 deserve special mention:

1. The Municipality net assets decreased by \$4,754,912.
2. In the fund financial statements, the governmental activities revenues decreased \$2,830,132 (or 5%) while governmental activities expenditures decreased \$3,877,227 (or 5%) in comparison with prior year.
3. The general fund (the primary operating fund) reflected, on a current financial resource basis, an increase of \$4,991,851.
4. On a budgetary basis, actual expenditures exceeded actual revenues by \$5,037,482, caused mainly due to unfavorable variances in both, revenues and expenditures accounts.
5. As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$18,813,380.
6. As the end of the current fiscal year the Municipality's General Fund deficit amounted to \$9,680,573, compared to a deficit of \$4,688,722 in the prior fiscal year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2009

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2009. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

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

FINANCIAL STATEMENTS COMPONENTS

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

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

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

A brief review of The Statements of Activities of the Municipality at June 30, 2009, shows total expenses incurred to afford the cost of all functions and programs amounted to \$64,212,423. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$23,364,000 was derived from the following sources: \$935,714 charges for services; \$19,254,554 from operating grants and contributions; and \$3,173,732 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$40,848,423.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2009

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

There was a deficit of revenues over expenses in the amount of \$4,754,912 which decreased the figure of net assets attained at the end of the fiscal year.

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

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

INFRASTRUCTURE ASSETS

Historically, a significant group of infrastructure assets such as roads, bridges, traffic signals, underground pipes not associated with utilities, have not been recognized nor depreciated in the accounting records of the Municipality. GASB 34 requires that such type of assets be inventoried, valued and reported under the governmental column of the Government-Wide Statement. As of July 1, 2002, the Municipality commenced the prospective reporting of infrastructure assets. The Municipality expects to retroactively report historical costs of infrastructure assets during the fiscal year beginning on July 1, 2006.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

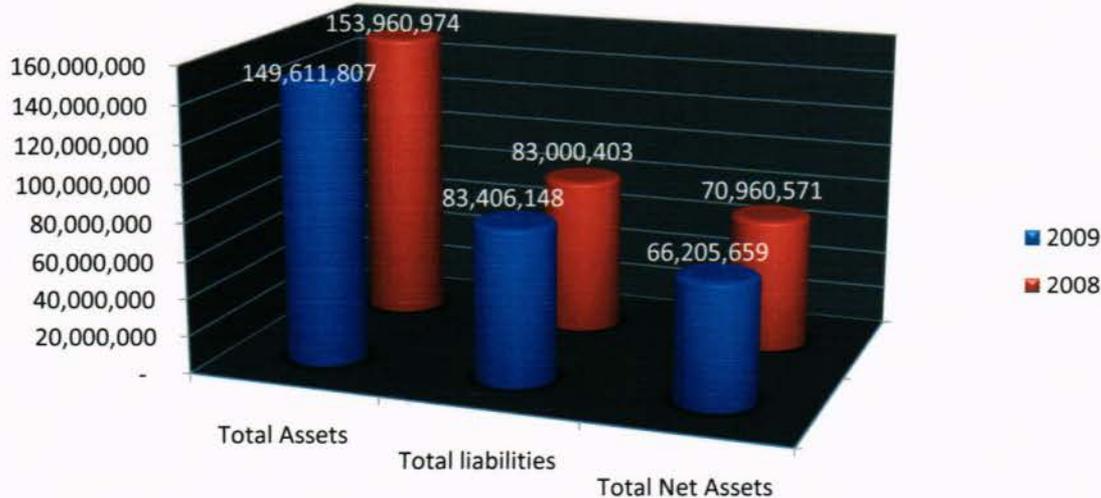
YEAR ENDED JUNE 30, 2009

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the **Municipality of Arecibo**, primary government total assets exceeded total liabilities by \$66,205,659 at the end of 2009, compared to \$70,960,571 at the end of the previous year and showed in the following condensed Statement of Net Assets of the Primary Government.

Condensed Statement of Net Assets	2009	2008	Change	%
Current and other assets	\$ 30,800,531	\$ 35,308,394	\$ (4,507,863)	(13%)
Capital Assets	118,811,276	118,652,580	158,696	0%
Total Assets	149,611,807	153,960,974	(4,349,167)	(3%)
Current and other liabilities	13,782,540	12,807,656	974,884	8%
Long-term liabilities	69,623,608	70,192,747	(569,139)	(1%)
Total liabilities	83,406,148	83,000,403	405,745	0%
Invested in capital assets, net of related debt	95,290,276	93,941,580	1,348,696	1%
Restricted	27,717,436	24,684,484	3,032,952	12%
Unrestricted deficit	(56,802,053)	(47,665,493)	(9,136,560)	19%
Total net assets	\$ 66,205,659	\$ 70,960,571	\$ (4,754,912)	(7%)



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2009

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Changes in Net Assets

The Statement of Activities reflects that for fiscal year 2009, the net effect of revenues derived from several programs plus current operating revenues compared to the total expenses, amounted to a decrease of \$4,754,912 in the Municipality's net assets. Approximately 49 percent of the Municipality's total revenue came from taxes, while 48 percent resulted from grants and contributions, including federal aid. Charges for services provided 2 percent and interest revenue, 1 percent. The Municipality's expenses cover a range of services. The largest expenses were for general government, health and welfare services, and public works. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

Condensed Statement of Activities	2009	2008	Change	%
Program revenues:				
Charges for services	\$ 935,714	\$ 1,165,696	\$ (229,982)	(20%)
Operating grants and contributions	19,254,554	19,753,321	(498,767)	(3%)
Capital grants and contributions	3,173,732	6,829,095	(3,655,363)	(54%)
General revenues:				
Property taxes	14,075,937	14,502,203	(426,266)	(3%)
Municipal license tax	13,509,878	12,782,776	727,102	6%
Municipal sales and use tax	3,897,513	3,009,940	887,573	29%
Grants and contributions not restricted to specific programs	7,844,772	8,449,623	(604,851)	(7%)
Other local taxes	931,800	710,099	221,701	31%
Interest and investment earnings	473,596	1,001,322	(527,726)	(53%)
Miscellaneous	114,927	773,205	(658,278)	(85%)
Total revenues	64,212,423	68,977,280	(4,764,857)	(7%)
Expenses:				
General government	26,715,928	25,840,044	875,884	3%
Public safety	4,339,434	3,959,450	379,984	10%
Public works	14,479,368	12,690,688	1,788,680	14%
Health and welfare	15,976,288	20,054,883	(4,078,595)	(20%)
Culture and recreation	1,552,520	1,314,233	238,287	18%
Economic development	4,825	15,526	(10,701)	(69%)
Community development	3,435,867	2,477,368	958,499	39%
Urban development	324,435	482,260	(157,825)	(33%)
Education	6,065	20,499	(14,434)	(70%)
Interest on long-term debt	2,132,605	2,577,295	(444,690)	(17%)
Total expenses	68,967,335	69,432,246	(464,911)	(1%)
Change in net assets	(4,754,912)	(454,966)	(4,299,946)	945%
Net assets, beginning	70,960,571	71,415,537	(454,966)	(1%)
Net assets, end of year	\$ 66,205,659	\$ 70,960,571	\$ (4,754,912)	(7%)

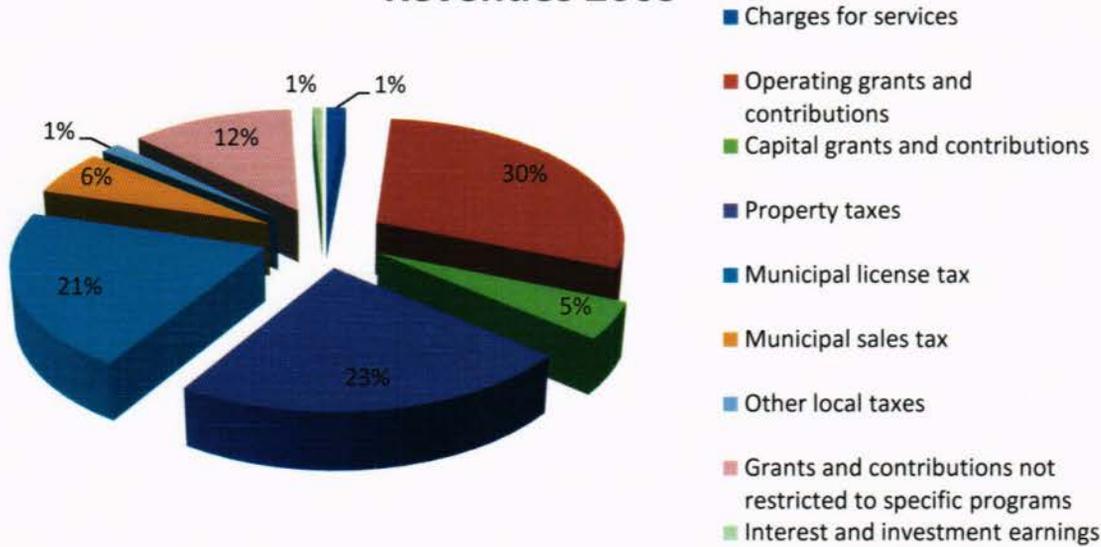
COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

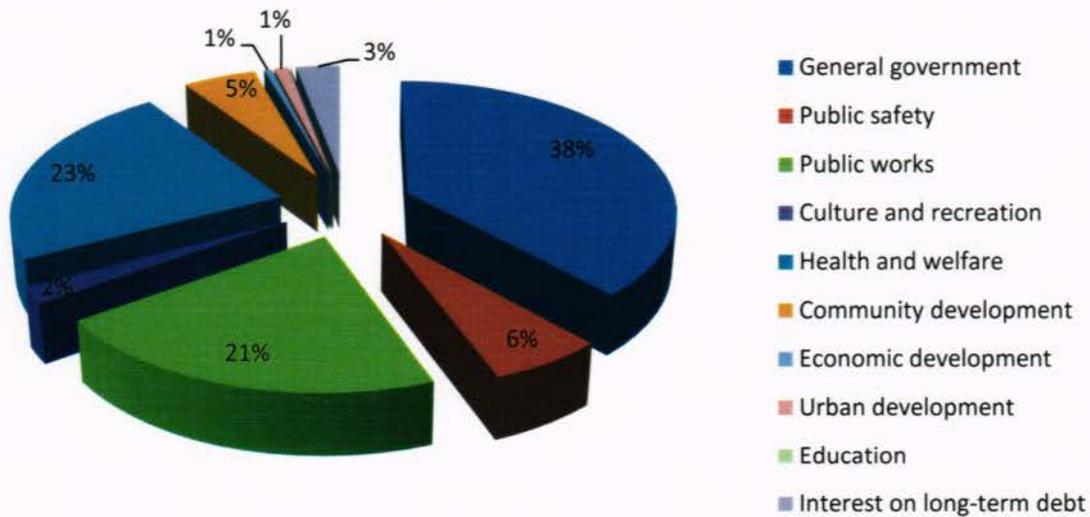
YEAR ENDED JUNE 30, 2009

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Revenues 2009



Expenses 2009



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2009

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$18,813,380, a decrease of \$2,397,405 in comparison with the prior year. There are reservations of fund balance amounting to \$30,231,317. This is the fund balance that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior fiscal year \$1,056,308, 2) to pay debt service \$5,970,327, 3) to pay for capital projects \$20,997,145, 4) for other purposes \$1,526,481, and, 5) for advances to other funds \$681,056.

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2009, the general fund has an undesignated fund balance of \$(11,417,937).

GENERAL FUND BUDGETARY HIGHLIGHTS

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

The actual General Fund budgetary activities resulted in an unfavorable balance of \$5,037,482 caused mainly by unfavorable variances in collections.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2009, amounts to \$154,854,742, which upon deduction of accumulated depreciation of \$36,043,466; produce a net book value of \$118,811,276. This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2009

CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2009, the Municipality has \$7,493,554 of unexpended proceeds mainly from bond and notes issuances that are committed to future construction activities.

Debt Administration

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

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

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

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

The American Recovery and Reinvestment Act of 2009, abbreviated ARRA, is an economic stimulus package endorsed by the President of the United States of America and approved by Congress.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2009

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

Its immediate goals include the creation of new jobs as well as save existing ones, preserve the economic activity, invest in long-term economic growth, and promote a high level of accountability and transparency in government spending.

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

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

FINAL COMMENTS

The Municipality is an autonomous governmental entity whose powers and authority vested on its Executive and Legislative Branches are specifically established in the Municipal Autonomous Act approved in August 1991. By virtue of such powers, it provides a wide range of services to its constituents which includes, among others, public works, education, public safety, public housing, health, community development, recreation, waste disposal, welfare and others.

The Municipality's principal sources of revenues are derived from property taxes, municipal license taxes, subsidies from the Commonwealth of Puerto Rico's General Fund and contributions from the Traditional and Electronic Lottery sponsored by said Government.

On September 7, 2004, Public Law 255 was enacted amending Public Law 83 of May 2, 1941, as amended. In addition to the new formula established for the calculation of the contribution in lieu of taxes as described in Note 1 (E) (2), applicable on fiscal year 2002-2003 and each subsequent fiscal year, the Law provides for quarterly revisions to be prepared by PREPA of its estimates corresponding to the contribution in lieu of taxes for the current fiscal year.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2009

FINAL COMMENTS (CONTINUED)

On August 12, 2005, the **Municipality of Arecibo** authorized the sale of the Puerto Rico Distillers for the amount of \$3,000,000. A non-interest bearing Note Receivable for a period of ten (10) years was issued by contract for a total of \$2,850,000. During the month of August, 2005 the Municipality collected \$150,000 corresponding to the down payment. The remaining balance was recognized as a Note Receivable in the government-wide financial statements. During fiscal year 2008-2009, the buyer paid \$1,940,850. The remaining receivable amounts to \$909,150.

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. Such has been the case of the financial operation corresponding to fiscal year 2009. It further contemplates to improve its current figure of net assets, which has been identified as one of the main short and long-term objectives of the Municipality.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at PO Box 1086, Arecibo, Puerto Rico 00613, or call (787) 878-5612.

Commonwealth of Puerto Rico
Municipality of Arecibo
Statement of Net Assets
June 30, 2009

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 15,089,775
Cash with fiscal agent	13,011,580
Accounts receivable:	
Municipal sales tax	36,862
Intergovernmental	452,301
Federal grants	1,127,462
Others	173,401
Notes receivable	909,150
Capital assets	
Land, improvements, and construction in progress	60,684,510
Other capital assets, net of depreciation	58,126,766
Total capital assets	<u>118,811,276</u>
Total assets	<u>149,611,807</u>
Liabilities	
Accounts payable and accrued liabilities	7,041,242
Due to other governmental entities	245,013
Deferred revenues:	
Municipal license tax	5,269,343
Federal grant revenues	450,425
Interest payable	776,517
Noncurrent liabilities:	
Due within one year	6,317,908
Due in more than one year	63,305,700
Total liabilities	<u>83,406,148</u>
Net Assets	
Invested in capital assets, net of related debt	95,290,276
Restricted for:	
Capital projects	20,997,145
Debt service	5,193,810
Other purposes	1,526,481
Unrestricted (deficit)	<u>(56,802,053)</u>
Total net assets	<u>\$ 66,205,659</u>

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

**Commonwealth of Puerto Rico
Municipality of Arecibo
Statement of Activities
For the Year Ended June 30, 2009**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and
		Charges for	Operating	Capital	Changes in Net Assets
		Services	Grants and	Grants and	Governmental
			Contributions	Contributions	Activities
General government	\$26,715,928	\$ 572,904	\$ 829,713	\$ -	\$ (25,313,311)
Public safety	4,339,434	174,193	342,380		(3,822,861)
Public works	14,479,368	185,067	2,425,700	2,467	(11,866,134)
Health and welfare	15,976,288		15,642,311		(333,977)
Culture and recreation	1,552,520	3,550			(1,548,970)
Economic development	4,825				(4,825)
Community development	3,435,867			3,171,265	(264,602)
Urban development	324,435		14,450		(309,985)
Education	6,065				(6,065)
Interest on long-term debt	2,132,605				(2,132,605)
Total governmental activities	\$68,967,335	\$ 935,714	\$19,254,554	\$ 3,173,732	(45,603,335)
General revenues:					
					14,075,937
Property taxes					13,509,878
Municipal license tax					3,897,513
Municipal sales tax					931,800
Other local taxes					7,844,772
Grants and contributions not restricted to specific programs					473,596
Interest and investment earnings					114,927
Miscellaneous					
Total general revenues					40,848,423
Change in net assets					(4,754,912)
Net assets - beginning					70,960,571
Net assets - ending					\$ 66,205,659

Commonwealth of Puerto Rico
Municipality of Arecibo
Balance Sheet
Governmental Funds
June 30, 2009

	General Fund	Special Revenue Fund Head Start	Special Revenue Fund Other Federal Grants	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Assets							
Cash and cash equivalents	\$ -	\$ 94,027	\$ 742,511	\$ 12,301,066		\$ 1,952,171	\$ 15,089,775
Cash with fiscal agent				7,493,554	5,518,026		13,011,580
Accounts receivable:							
Municipal sales tax						36,862	36,862
Intergovernmental					452,301		452,301
Federal grants		9,279	1,118,183				1,127,462
Others	166,439					6,962	173,401
Advances from other funds	681,056						681,056
Due from other funds	1,054,082			1,413,759			2,467,841
Total assets	\$ 1,901,577	\$ 103,306	\$ 1,860,694	\$ 21,208,379	\$ 5,970,327	\$ 1,995,995	\$ 33,040,278
Liabilities and Fund Balances							
Liabilities :							
Accounts payable and accrued liabilities	\$ 4,765,502	\$ 90,640	\$ 231,445	\$ 25,633	\$ -	\$ -	\$ 5,113,220
Due to other governmental entities	245,013						245,013
Advances to other funds			479,482			201,574	681,056
Due to other funds	1,302,292		712,008	185,601		267,940	2,467,841
Deferred revenues:							
Municipal license tax	5,269,343						5,269,343
Federal grant revenues		12,666	437,759				450,425
Total liabilities	11,582,150	103,306	1,860,694	211,234	-	469,514	14,226,898
Fund balances:							
Reserved for:							
Encumbrances	1,056,308						1,056,308
Capital projects				20,997,145			20,997,145
Debt service fund					5,970,327		5,970,327
Advances to other funds	681,056						681,056
Other purposes						1,526,481	1,526,481
Unreserved:							
Undesigned	(11,417,937)						(11,417,937)
Total fund balances	(9,680,573)			20,997,145	5,970,327	1,526,481	18,813,380
Total liabilities and fund balances	\$ 1,901,577	\$ 103,306	\$ 1,860,694	\$ 21,208,379	\$ 5,970,327	\$ 1,995,995	

Amounts reported for governmental activities in the statement of net assets are different because:

Accrual basis of accounting accounts receivable recognized in government-wide financial statements	909,150
Accrual basis of accounting accounts payable recognized in government-wide financial statements	(1,928,022)
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	118,811,276
Long-term liabilities, including accrued interest payable, are not due and payable in the current period, and therefore, are not reported in the funds	(70,400,125)
Net assets of governmental activities	\$ 66,205,659

Commonwealth of Puerto Rico
Municipality of Arecibo
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2009

	General Fund	Special Revenue Fund Head Start	Special Revenue Fund Other Federal Grants	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Revenues							
Property taxes	\$ 11,372,444	\$ -	\$ -	\$ -	\$ 2,703,492	\$ -	\$ 14,075,936
Municipal license taxes	13,509,878						13,509,878
Municipal sales taxes					608,436	3,289,077	3,897,513
Licenses, permits and other local taxes	931,800						931,800
Charges for services	104,348					7,131	111,479
Intergovernmental	8,674,486			2,428,167		405,765	11,508,418
Fines and forfeitures	174,193						174,193
Rent of property	551,744			98,300			650,044
Interest	473,596						473,596
Federal grants		8,555,439	5,996,619			4,212,583	18,764,641
Miscellaneous	2,041,700			440		6,962	2,049,102
Total revenues	37,834,189	8,555,439	5,996,619	2,526,907	3,311,928	7,921,518	66,146,600
Expenditures							
Current:							
General government	29,586,719					171	29,586,890
Public safety	4,156,673		146,260			112,834	4,415,767
Public works	11,107,180			2,930,693			14,037,873
Health and welfare		8,791,163	2,659,570			4,463,844	15,914,577
Culture and recreation	966,511			136,168		8,356	1,111,035
Economic development						4,725	4,725
Community development			3,179,839				3,179,839
Urban development			14,450	88,000		217,738	320,188
Debt service:							
Principal					2,437,000		2,437,000
Interest					2,571,111		2,571,111
Total expenditures	45,817,083	8,791,163	6,000,119	3,154,861	5,008,111	4,807,668	73,579,005
Excess (deficiency) of revenues over (under) expenditures	(7,982,894)	(235,724)	(3,500)	(627,954)	(1,696,183)	3,113,850	(7,432,405)
Other financing sources (uses)							
Transfers in	4,425,174	235,724	3,500		1,194,907		5,859,305
Transfers out	(1,434,131)					(4,425,174)	(5,859,305)
Long-term debt issued				5,035,000			5,035,000
Total other financing sources (uses)	2,991,043	235,724	3,500	5,035,000	1,194,907	(4,425,174)	5,035,000
Net change in fund balances	(4,991,851)			4,407,046	(501,276)	(1,311,324)	(2,397,405)
Fund balance, beginning	(4,688,722)	-	-	16,590,099	6,471,603	2,837,805	21,210,785
Fund balance, ending	\$ (9,680,573)	\$ -	\$ -	\$ 20,997,145	\$ 5,970,327	\$ 1,526,481	\$ 18,813,380

Handwritten signature and date: 6/30/09

Commonwealth of Puerto Rico
Municipality of Arecibo
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2009

Net Change in Fund Balances - Total Governmental Funds	\$ (2,397,405)
Amounts reported for governmental activities in the Statement of Activities are different because:	
Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds. The following amount represents the change in this revenue from prior year.	(1,940,850)
Governmental Funds report capital outlays as expenditures. However in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period.	3,385,176
Donations of Capital Assets from outside parties, do not provide current financial resources in Governmental Funds, but the transaction must be reflected in the Government-Wide Statement of Net Assets based on the fair value of the donated property,	6,675
Retirement of Capital assets	(2,475)
Depreciation Expense on Capital Assets is reported in the Government-Wide Statements of Activities and Change in Net Assets, but they do not require the use of current financial resources. Therefore, Depreciation expense is not reported as expenditures in Governmental Funds Financial Statements.	(3,230,680)
Interest Expense change is reported in the Government-Wide Statement of Activities and Change in Net Assets, but not require the use of current financial resources. Therefore, Interest expense change is not reported as expenditures in Governmental Funds Financial Statements.	438,506
Accounts payable change reported in the Government-Wide Statement of Activities and Change in Net Assets but not reported as in the Governmental Funds because they do not require the use of current financial resources. This is the amount reported in the current period.	(1,582,998)
Long term debt issuances are reported in the Government-Wide Statement of Net Assets, but not require the use of current financial resources. Therefore, Long term debt issuances are not reported as expenditures in Governmental Funds Financial Statements.	(4,590,423)
Long term debts payments are reported as expenditures in the Governmental Funds Financial Statements which require the use of current financial resources. Therefore Long term debt payments are not reported as expenditures in the Government-Wide Statement of Activities and Change in Net Assets.	1,907,875
Change in Landfill Accrual	5,848,687
Bonds proceeds provide current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide statement of Net Assets. Repayment of bond principal is an expenditure in Governmental Funds, but the repayment reduces long -term liabilities in the Government-Wide Statement of Net Assets. This is the amount by which the debt service principal payments exceed debt proceeds.	(2,597,000)
Change in Net Assets of Governmental Activities	\$ (4,754,912)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Arecibo** (the Municipality) was founded on the year 1515. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a sixteen member Municipal Legislature who are elected for a four-year term.

The Municipality provides public safety, public works, culture and recreation, health and welfare, community development, education, and other miscellaneous services.

The accounting policies and financial reporting practices of the Municipality conform to accounting principles generally accepted in the United States of America ("USGAAP") as applicable to governmental units.

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's and Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. The Statement was adopted as of July 1, 2002. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

As part of this Statement, there is a new reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). This requirement permits an optional four-year delay for implementation to fiscal year 2007. The Municipality implemented the capitalization of infrastructure since July 1, 2006.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

A. Component Units

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, The Financial Reporting Entity, of the GASB. As amended by the GASB Statement No. 39, "Determining Whether Certain Organizations Are Component Units, an amendment of GASB Statement 14". The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. USGAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

"Corporación Desarrollo Cultural Teatro Oliver C.E." is a non-profit organization duly organized and existent under the laws of the Commonwealth of Puerto Rico. It was established to acquire, restore and operate the Teatro Oliver of Arecibo, Puerto Rico.

The Municipality management determined as a component unit the operations of Teatro Oliver, because of the financial interdependency, ability to designate management and the ability to significantly influence operations demonstrated by the Municipality. The Theater funds becomes from private and municipal donations and the rent of the facilities.

The "Corporación Desarrollo Cultural Teatro Oliver C.E." elected the provision of Section 101 (7) of the Puerto Rico Income Tax Law for non-profit organization and all of their net revenues are exempt from the payment of income taxes.

B. Government-wide and fund financial statements

Financial information of the Municipality is presented in this report as follow:

1. Management's discussion and analysis introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all the activities of the Municipality and its component units, if any. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-typed activities, if any, which rely to a significant extent on fees and charges for support. Interfund activity has been removed from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenue. Direct expenses are those that are charges to customers of applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The Municipality reports the following major governmental funds:

General Fund- is the accounting entity in which all governmental activity, except that which is required to be accounted for in another fund, is accounted for. Its revenues consist mainly of taxes, licenses and permits, intergovernmental revenue, charges for services and other.

Special Revenue Fund - Head Start- is the accounting entity in which revenues derived from the federal agency are used to provide comprehensive health, educational, nutritional, social, and other developmental services primarily to economically disadvantaged preschool children (ages 3 to 5) and infants and toddler (birth through age 3) so that the children will attain school readiness.

Special Revenue Fund - Other Federal Grants- is the accounting entity in which revenues derived from federal grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal statutes.

Capital Projects Fund - State and Local Grants- is the accounting entity in which revenues derived from local funds, state or other restricted revenue sources related to capital projects, is accounted for. The uses and limitations of each capital project fund are specified by Municipality ordinances or federal and state statutes.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Debt Service Fund - is the accounting entity used to account for the resources accumulated and payments made for principal and interest on long-term general obligation bonds of governmental funds.

4. The notes to the financial statements provide information that is essential to a user's understanding of the basic financial statements.
5. Required supplementary information such as the budgetary comparison schedule-general fund and other types of data required by GASB.
6. Notes to the budgetary comparison schedule-general fund.

C. Financial reporting presentation

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Fund types are as follows:

General Fund - Is the operating fund of the Municipality. It is used to account for all governmental activity, except those required to be accounted for in another fund.

Special Revenue Fund - Local and State Grants - Special Revenue Funds are used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Section 8 - Special Revenue Fund used to account for revenues derived from Section 8 Housing Choice Voucher Program. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Head Start- Is the accounting entity in which revenues derived from the federal agency are used to provide comprehensive health, educational, nutritional, social, and other developmental services primarily to economically disadvantaged preschool children (ages 3 to 5) and infants and toddler (birth through age 3) so that the children will attain school readiness.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Special Revenue Fund - Other Federal Grants - Special Revenue Funds are used to account for revenues derived from federal grants. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Projects Funds - Local, State and Federal Grants - Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

Debt Service Funds- Debt Service Funds are used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

D. Measurement focus, basis of accounting and financial presentation

Except for budgetary purposes, the basis of accounting used by the Municipality conform to accounting principles generally accepted in the United States of America ("USGAAP") as applicable to governmental units. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The Municipality has elected not to apply all Statements and Interpretations issued by the Financial Accounting Standard Board after November 30, 1989, in accordance with GASB Statement No.20.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds from issuance of general long-term debt reported as other financing sources.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property taxes, other taxes, licenses, rent, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

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

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants, and contributions, and 3) capital grants and contributions, including special assessments, if any. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

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

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

E. Assets, liabilities and net assets

1. Cash, cash equivalents, and cash with fiscal agent- The Municipality's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

Cash with fiscal agent in the debt service fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law. Also, cash with fiscal agent consists of unused proceeds of bond and notes issued for the acquisition of equipment and construction of major capital improvements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

- 2. Receivables and payables-** 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 fund financial statements, if any, 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.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivable in the general fund relates mostly to Law 52 proposal payroll reimbursements from prior years and property taxes owed by the Municipal Revenue Collection Center ("CRIM"). Intergovernmental receivable in the debt service fund represent property taxes owed by the Municipal Revenue Collection Center ("CRIM").

- 3. Inventories-** Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.
- 4. Capital assets-** Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets of the Municipality are depreciated using the straight-line method over the following estimated useful lives:

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Buildings and site improvements	40 years	\$1
Infrastructure	40 years	\$1
Works of art	10 years	\$1
Vehicles	5 years	\$1
Furniture and fixtures	5 years	\$25
Machinery and equipment	3 to 5 years	\$25

- 5. Long-term obligations-** The liabilities reported in the government-wide financial statements include to general and special obligation bonds and notes, and other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

- 6. Compensated absences-** Employees accumulate vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. All vacation pay it is accrued when incurred in the government-wide financial statements.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality. All sick leave pay and salary related benefits are accrued when incurred in the governmental-wide financial statements when the employee meets such criteria.

- 7. Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund when the liability is incurred.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

8. **Reservations of fund balance-** Reservations of fund balance in the fund financial statements represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:

- a. **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.
- b. **Encumbrances-** Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
- c. **Other Purposes-** Represents net assets available for specific use and/or legally segregated for other specific future use.
- d. **Debt Service Fund-** Represents net assets available to finance future debt service payments.

9. **Interfund and intra-entity transactions-** The Municipality has the following types of transactions among funds:

- a. **Operating Transfers-** Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
- b. **Intra-Entity Transactions-** Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.

10. **Risk financing-** The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the CRIM for the year ended June 30, 2009 amounted to \$865,260. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$1,024,969 for workers compensation insurance covering all municipal employees.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

11. Reconciliation of Government-wide and Fund Financial Statements

The governmental fund balance sheet includes reconciliation between fund balance-total governmental funds and net assets-governmental activities as reported in the government-wide statement of net assets. The two elements of that reconciliation explains that "long term liabilities, including compensated absences, bonds and notes payable, are not due and payable in the current period and therefore are not reported in the funds.", and that "capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. The details of this reconciliation are as follows:

		<u>Total Net Assets - Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 118,811,276	
Deduct:		
Bonds payable related to capital assets	(23,361,000)	
Notes payable related to capital assets	<u>(160,0000)</u>	\$ 95,290,276
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		20,997,145
<u>Net assets restricted for debt service</u>		
Fund balance restricted for debt service	5,970,327	
Deduct:		
Interest Payable	<u>(776,517)</u>	5,193,810
<u>Net assets restricted for other purposes</u>		
Other governmental funds - Fund balance restricted for other purposes		1,526,481
<u>Net assets unrestricted (deficit)</u>		
General fund - total fund balance:	(9,680,573)	
<u>Add:</u>		
Accrual basis accounts receivable	909,150	
<u>Deduct:</u>		
Accrual basis accounts payable	(1,928,022)	
Bonds Payable related to operational debts	(25,234,000)	
Compensated absences debt	(7,271,637)	
Landfill obligation	(7,257,543)	
LIMS Repayment Plan	(502,921)	
Property tax debt - Law 42	(1,164,874)	
Property tax debt - Law 146	(1,008,506)	
Property tax debt - Final Liquidation 2006-2007, 2007-2008, 2008-2009	(921,012)	
Retirement System Administration	(798,383)	
State Insurance Fund Payment Plan	(131,489)	
Claims and judgments debt	<u>(1,812,243)</u>	<u>(56,802,053)</u>
Total net assets - governmental activities		<u>\$ 66,205,659</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

2. CASH AND CASH EQUIVALENTS

The Municipality maintains its deposits in various commercial banks located in Puerto Rico and Government Development Bank for Puerto Rico (GDB). Proceeds from bonds and funds related to certain grant awards are required by law to be held with GDB.

The Municipality adopted the provisions of GASB Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate risk, (3) custodial credit risk, (4) foreign exchange exposure.

Credit risk – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2009.

Interest rate risk – This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2009, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. At June 30, 2009, the Municipality's investments in certificates of deposits are recorded at cost, which approximates their fair value. Therefore, the Municipality's management has concluded that at June 30, 2009, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

Custodial credit risk – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$100,000 per depositor.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

2. CASH AND CASH EQUIVALENTS (CONTINUED)

Custodial credit risk -In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2009. Therefore, the Municipality's management has concluded that at June 30, 2009 the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign exchange risk - The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2009.

Under Commonwealth of Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The Municipality's bank balances in commercial banks of \$94,027, \$742,511, \$12,301,066, and \$1,952,171 in the special revenue fund-Head Start, special revenue fund-other federal grants, capital projects fund-local and state grant, and in other governmental funds, respectively, were fully collateralized at June 30, 2009. Also, in the general fund, there are \$5,500,000 deposited in a savings and loan institution, \$5,250,000 from that amount are unsecured and uncollateralized, since (COSSEC) insures up to \$250,000 of deposits in such institutions.

The deposits at GDB of \$7,493,554 that are restricted principally for capital projects in the capital project fund - local and state grant, and the \$5,518,026 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

A. Municipal License Tax- The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Act of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

3. RECEIVABLES (CONTINUED)

During the fiscal year ended June 30, 2009, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues
2. Other organizations- 0.50% of gross revenues

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 24. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2009, net of allowance for uncollectibles.

Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

- B. *Municipal Sales Tax*** - On July 29, 2007, an amended to Act No. 117 of July 4, 2006, known as the "Tax Fairness Act of 2006", was enacted with the purpose of establishing a mandatory sales and use tax of 1.5% at the Municipal Level. The Municipalities of Puerto Rico are responsible to collect 1% of the corresponding tax with the same exemptions and limitations that the portion collected by the Treasury Department. The Act provides an optional surtax on the un-process food. This surtax must be approved by the Municipal Legislature. The Treasury Department is responsible to create the Municipal Development Fund (.2%), the Municipal Redemption Fund (.2%) and the Municipal Improvements Fund (.1%) with the remaining 0.5%. The Municipality collected \$3,289,077 during the year ended June 30, 2009. This amount is deposited in other governmental funds. Also, \$910,429 from the Municipal Redemption Fund are included in the debt service fund. Municipal sales and use tax receivable of \$36,862, in the other governmental funds represents filed tax returns that were uncollected as of June 30,2009, net of allowance for uncollectible accounts.
- C. *Intergovernmental*** - Intergovernmental receivable in the debt service fund represents the amounts due from the CRIM resulting from the excess of the current year property tax collections over current year advances. Following is a detail of the Intergovernmental receivable:

<u>Program Description</u>	<u>Amount</u>
Municipal Revenue Collection Center ("CRIM")	\$ <u>452,301</u>
Total	\$ <u>452,301</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

3. RECEIVABLES (CONTINUED)

D. **Federal grants-** Federal grants receivable in the special revenue fund-Head Start represents expenditures incurred not yet reimbursed by the Federal government. Following is a detail of the federal grants receivable:

<u>Program Description</u>	<u>Amount</u>
Head Start Program	\$ 9,279
Total	<u>\$ 9,279</u>

Federal grants receivable in the special revenue fund-other federal grants represent expenditures incurred not yet reimbursed by the Federal government. Following is a detail of the federal grants receivables:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grant/Entitlement Grants	\$ 162,692
Public Assistance Grant	265,528
Community Service Block Grant	41,364
Special Program for Aging - Title III	49,670
Child Care Development Block Grant Program	403,779
Even Start Family Literacy Program	25,241
Homeland Security Grant Program	<u>169,909</u>
Total	<u>\$ 1,118,183</u>

E. **Note Receivable-** In August 2005, the Municipal Legislature authorized the Mayor to sell the Puerto Rico Distiller facilities for a sale price of \$3,000,000. In the prior year, the Municipality collected a down payment of \$150,000.

The buyer could at any time make payments of the remaining balance of the note receivable of \$2,850,000, during the term of ten years, as stipulated by contract. The payments could be divided depending of the development of the project phases or could be made in a single payment as long as it is in the established term. During fiscal year 2008-2009, the buyer paid \$1,940,850. The remaining receivable amounts to \$909,150.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2009, and interfund transfers during the fiscal year ended at June 30, 2009, are summarized as follows:

a. Due from/to other fund and Advances to/from other funds:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund-Other Federal Grants	Payroll and related accruals paid and not reimbursed	\$1,191,490
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed	358,047
General Fund	Capital Projects Funds	Reimbursable Expenditures	185,601
Capital Projects Fund	Other Governmental Funds	Reimbursable Expenditures	111,467
Capital Projects Fund	General Fund	Reimbursable transfer of funds	<u>1,302,292</u>
Total			<u>\$ 3,148,897</u>

b. Transfer in/out to other fund

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Debt Service Fund	Debt Retirement	\$ 1,194,907
General Fund	Special Revenue Fund-Head Start	In-kind Cash Contribution	235,724
General Fund	Special Revenue Fund-Other Federal Grants	Transfer of funds to finance operations	3,500
Other Governmental Funds	General Fund	Transfer of funds to finance operations	<u>4,425,174</u>
Total			<u>\$ 5,859,305</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

5. CAPITAL ASSETS

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2009, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<u>Governmental Activities:</u>	<u>Balance July 1, 2008</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance June 30, 2009</u>
Capital asset, not being depreciated:				
Construction in progress	\$ 7,990,361	\$ 1,477,085	\$ (3,479,041)	\$ 5,988,405
Land	<u>54,607,121</u>	<u>88,984</u>	<u>-</u>	<u>54,696,105</u>
Total capital assets not being depreciated	<u>62,597,482</u>	<u>1,566,069</u>	<u>(3,479,041)</u>	<u>60,684,510</u>
Capital assets, being depreciated:				
Buildings	44,193,249	553,787	-	\$ 44,747,036
Buildings improvements	9,998,622	841,276	-	10,839,898
Infrastructure	16,529,931	73,200	-	16,603,131
Infrastructure improvements	4,485,102	2,232,803	-	6,717,905
Equipment	3,857,632	478,150	(31,756)	4,304,026
Furnishing	1,662,617	54,661	(32,212)	1,685,066
Computers	635,826	184,648	(42,673)	777,801
Works of Art	210,344	6,675	(68,378)	148,641
Vehicles	<u>7,467,134</u>	<u>879,623</u>	<u>(29)</u>	<u>8,346,728</u>
Total capital assets being depreciated	<u>89,040,457</u>	<u>5,304,823</u>	<u>(175,048)</u>	<u>94,170,232</u>
Less accumulated depreciation for:				
Buildings	(9,731,336)	(1,118,676)	-	(10,850,012)
Buildings improvements	(857,789)	(265,022)	-	(1,122,811)
Infrastructure	(9,990,234)	(414,469)	-	(10,404,703)
Infrastructure improvements	(381,888)	(402,671)	-	(784,559)
Equipment	(3,127,720)	(336,037)	30,888	(3,432,869)
Furnishing	(1,534,093)	(57,346)	31,693	(1,559,746)
Computers	(555,521)	(74,160)	42,606	(587,075)
Work of Art	(195,696)	(8,697)	67,357	(137,036)
Vehicles	<u>(6,611,082)</u>	<u>(553,602)</u>	<u>29</u>	<u>(7,164,655)</u>
Total accumulated depreciation	<u>(32,985,359)</u>	<u>(3,230,680)</u>	<u>172,573</u>	<u>(36,043,466)</u>
Total capital assets being depreciated, net	<u>56,055,098</u>	<u>2,074,143</u>	<u>(2,475)</u>	<u>58,126,766</u>
Governmental activities capital assets, net	<u>\$ 118,652,580</u>	<u>\$ 3,640,212</u>	<u>\$ (3,481,516)</u>	<u>\$118,811,276</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

5. CAPITAL ASSETS (CONTINUED)

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

Governmental activities:

General Government	\$ 668,985
Public Safety	136,153
Public Works	1,115,849
Health and Welfare	23,895
Culture and Recreation	820,411
Economic Development	100
Community Development	454,973
Urban Development	4,249
Education	<u>6,065</u>

Total depreciation expense-governmental activities \$ 3,230,680

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2009 are summarized as follows:

<u>Description</u>	<u>General Fund</u>	<u>Special Revenue Fund - Head Start</u>	<u>Special Revenue Fund - Other Federal Grants</u>	<u>Capital Projects Fund - State & Local Grants</u>	<u>Debt Service Fund</u>	<u>Other Governmental Fund</u>	<u>Total</u>
Accounts payable	\$ 792,351	\$ 90,640	\$ 231,445	\$ 25,633	\$ -	\$ -	\$ 1,140,069
Bank overdraft	3,973,151						3,973,151
Accrued liabilities	-	-	-	-	-	-	-
Total	<u>\$ 4,765,502</u>	<u>\$ 90,640</u>	<u>\$ 231,445</u>	<u>\$ 25,633</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 5,113,220</u>

7. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the CRIM, a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomous Law of August 1991. Real property tax is assessed by the CRIM on each piece of real estate and on each building.

1. The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

7. PROPERTY TAXES (CONTINUED)

ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, 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 three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. As of June 30, 2008, the CRIM issued the final settlement noting that advances exceeded collections by \$389,998. This balance will be retained by the CRIM during fiscal year 2009-2010. In addition, the CRIM issued the final settlement noting that advances exceeded collections by \$531,014. This balance will be retained by the CRIM during fiscal year 2010-2011. Those amounts are presented in the government wide financial statements.

On January 26, 2000, Public Law No. 42 was enacted which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000.

The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238, enacted on August 15, 1999. On October 11, 2001, Public Law No. 146 was enacted to amend Public Law No. 42, to extend the loan amortization period up to 30 years. Also, on October 11, 2002, Public Law No. 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law No. 42 enacted on January 26, 2000.

On June 26, 1997, Public Law No. 21 was enacted which authorized the CRIM to sell property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. The property tax receivables were purchased by Public Financing Corporation, a subsidiary of the

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

7. PROPERTY TAXES (CONTINUED)

Government Development Bank (GDB), with proceeds of a bonds issuance. This Law imposes to the CRIM the obligation to replace any uncollectible property tax receivable with any valid property tax receivables or equivalent in money.

A high percentage of receivables were determined to be uncollectible receivables, and therefore, on October 11, 2001, Public Law No. 146 was enacted which authorized the CRIM to obtain a loan to pay in advance the bonds issued by the Public Financing Corporation (a GDB subsidiary), and any costs related to the transaction. Also, a term not to exceeding 30 years was authorized to the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from the sale of property tax receivables to the Public Financing Corporation (a GDB Subsidiary).

The government-wide statement of net assets includes an outstanding balance of \$1,164,874 and \$1,008,506 related to Law No. 42 and Law No. 146 respectively.

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

The annual tax rate is 8.58% for real property and 6.58% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund.

A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.75% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

8. DUE TO OTHER GOVERNMENTAL ENTITIES

The amounts due to other governmental entities in the General Fund include the following:

<u>Governmental Entity</u>	<u>Amount</u>
General Services Administration	\$ 16,839
Department of Labor	52,914
Treasury Department	4,228
Puerto Rico Aqueduct and Sewer Authority	<u>171,032</u>
Total	<u>\$ 245,013</u>

9. DEFERRED REVENUES

A. Municipal License Tax- The deferred revenues of \$5,269,343 in the general fund relates to municipal license tax collected in fiscal year 2008-09 that will be earned in fiscal year 2009-10.

B. Federal Grants- The deferred revenues presented in special revenue fund-Head Start program represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Child Care Food Program	<u>\$ 12,666</u>
Total	<u>\$ 12,666</u>

The deferred revenues presented in special revenue fund-other federal grants represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Rural Development Corporation	\$ 162,000
Federal Transit Authority	49,331
Community Development Block Grant/Entitlement Grants	67,088
Public Assistance Grant	129,761
Rural Domestic Violence and Child Victimization Enforcement Grant Program	4,696
Other	<u>24,883</u>
Total	<u>\$ 437,759</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

10. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2009, was as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds Payable	\$ 45,848,000	\$ 5,035,000	\$ (2,288,000)	\$ 48,595,000	\$ 2,453,000
Notes Payable	310,000		(150,000)	160,000	160,000
LIMS Repayment Plan	684,335		(181,414)	502,921	192,369
Property Tax Debt - Law 42	1,186,482		(21,608)	1,164,874	22,964
Property Tax Debt - Law 146	1,052,354		(43,848)	1,008,506	43,848
CRIM Final Liquidation 2008-2009		531,014		531,014	
CRIM Final Liquidation 2006-2007	69,651		(69,651)		
CRIM Final Liquidation 2007-2008	389,998			389,998	
Compensated Absences	5,920,530	1,854,111	(503,004)	7,271,637	1,755,855
Landfill Obligation	13,106,230		(5,848,687)	7,257,543	
Retirement System Administration Payment Plan-Special Laws	562,757	554,298	(318,672)	798,383	798,382
State Insurance Fund - Payment Plan	860,667		(729,178)	131,489	131,490
Claims and Judgments	201,743	1,651,000	(40,500)	1,812,243	760,000
Total	\$ 70,192,747	\$9,625,423	\$ (10,194,562)	\$69,623,608	\$ 6,317,908

- 1. Legal debt margin-** The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality plus 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 are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds and notes payable (excluding notes payable to the Land Authority), is paid with unrestricted funds.
- 2. Bonds Payable-** The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities and for the liquidation of operational debts. Bonds payable outstanding at June 30, 2009 are as follows:

<u>Type of bonds</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest Rates</u>	<u>Balance at June 30, 2009</u>
1987-Series	1-1-2012	875,000	5.00%	\$ 180,000
1989-Series	1-1-2014	500,000	5.00%	165,000
1994-Series	1-1-2019	400,000	4.87%	241,000
1995-Series	7-1-2020	14,975,000	6.05% to 6.63%	10,575,000
1998-Series	1-1-2023	900,000	4.75%	647,000
1999-Series	7-1-2024	7,365,000	3.54% to 5.60%	6,045,000
2001-Series	7-1-2026	10,545,000	7.00% to 8.00%	9,015,000
2002-Series	7-1-2026	5,030,000	3.54% to 5.60%	4,385,000
2003-Series	7-1-2028	4,235,000	6.00%	3,705,000
2004-Series	7-1-2013	360,000	5.00% to 6.00%	205,000
2004-Series	7-1-2028	605,000	5.00% to 6.00%	545,000
2004-Series	7-1-2013	294,000	6.00%	138,000
2004-Series	7-1-2029	410,000	4.17 to 4.73%	325,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

10. LONG-TERM LIABILITIES (CONTINUED)

<u>Type of bonds</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest Rates</u>	<u>Balance at June 30, 2009</u>
2004-Series	7-1-2029	\$ 1,610,000	4.00%	\$ 1,445,000
2005-Series	7-1-2014	7,670,000	5.50%	5,045,000
2006-Series	7-1-2017	1,056,000	6.62% to 7.00%	899,000
2009 Series	7-1-2034	1,015,000	2.43% to 7.50%	1,015,000
2009 Series	7-1-2034	4,020,000	4.75% to 7.50%	<u>4,020,000</u>
Total general obligation bonds				<u>\$ 48,595,000</u>

These bonds, except the 1989-Series amounting to \$3,000,000, 2001-Series amounting to 10,545,000, 2003-Series amounting to 4,235,000 and 2004-Series amounting \$294,000 are payable from the ad valorem property tax of 1.75% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

Annual debt service requirements to maturity for bonds payable are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2010	\$ 2,453,000	\$ 2,759,089
2011	2,616,000	2,872,110
2012	2,780,000	2,714,608
2013	2,912,000	2,546,061
2014	3,072,000	2,367,529
2015-2019	13,594,000	9,242,961
2020-2024	12,618,000	4,956,720
2025-2029	6,615,000	1,548,450
2030-2034	<u>1,935,000</u>	<u>364,725</u>
Total	<u>\$ 48,595,000</u>	<u>\$ 29,372,253</u>

- 3. Note Payable-** The proceeds of the issuance of the note payable was used principally to pay debt incurred in prior years and to cover the expenditures of a special event. The note is payable as follows:

<u>Type of notes</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest rates</u>	<u>Balance at June 30, 2009</u>
2003-Series	7-1-2009	\$ 920,000	3.88% to 4.10%	<u>\$ 160,000</u>
Total notes payable				<u>\$ 160,000</u>

This note is payable from the special ad valorem property tax of 1.75% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

Annual debt service requirements to maturity for notes payable are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2010	<u>\$ 160,000</u>	<u>\$ 3,280</u>
Total	<u>\$ 160,000</u>	<u>\$ 3,280</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

10. LONG-TERM LIABILITIES (CONTINUED)

- 4. LIMS Repayment Plan-** During the fiscal year 2001-2002, the Municipality authorized the CRIM to retain the corresponding portion for the financing project of Land Information Management System - LIMS, contracted by the CRIM. A total of \$1,636,386 is to be retained in a ten years period at an interest rate of 5.95%, until November 28, 2011. At June 30, 2009, the outstanding debt balance is \$502,921. This amount is presented in the government wide financial statements.
- 5. Property Tax Debt-** These amounts represent the balance owed to the Municipal Revenue Collection Center (CRIM) at June 30, 2009, as described in Note 7.
- 6. Compensated Absences-** The government-wide statement of net assets includes \$2,253,442 of accrued sick leave benefits, and \$5,018,195 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.
- 7. Landfill obligation-** State and federal laws and regulations require the Municipality to place a final cover on its landfill site when closed and perform certain maintenance and monitoring functions at the landfill site for 30 years after closure. In accordance with Statement No. 18 of the GASB, "Accounting for Municipal Solid Waste Landfill Closure and Post Closure Care Costs", the Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space. In addition to operating expenses related to the current activities of the landfill, an expense provision and related liability are being recognized based on the future closure and post-closure care cost that will be incurred near or after the date the landfill no longer accepts waste. The recognition of these landfill closure and post-closure care costs is based on the amount of landfill used during the year. During the fiscal year 2008-2009, the landfill administration made some capital improvements that changed the estimate. The estimated liability for landfill closure and post-closure care costs has a balance of \$7,257,543 as of June 30, 2009 reported in the Government-Wide Financial Statements, which is based on 51% usage (filled) of the landfill. It is estimated that an additional \$2,156,400 will be recognized as closure and post-closure care expenses between the date of the balance sheet and the date the landfill is expected to be filled to capacity (2015). The estimated total current cost of the landfill closure and post-closure care (\$12,000,000) is based on the amount that would be paid if all equipment, facilities and services required to close, monitor, and maintain the landfill were acquired as of June 30, 2009. However, the actual cost of closure and post-closure care may be higher due to inflation, changes in technology, or changes in landfill laws and regulations. The **Municipality of Arecibo** maintains \$452,070 in a bank account held for landfill improvements, and has a balance due from the general fund of \$1,000,000.
- 8. Retirement System Administration -** This amount represent a payment plan agreement with the governmental agency to pay Special Laws from prior years.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

10. LONG-TERM LIABILITIES (CONTINUED)

- 9. Claims and Judgments-** - These amounts represent the balance related to legal claims at June 30, 2009, as described in Note 15.

11. OPERATING LEASES

The Municipality is obligated under certain leases accounted for as operating leases. Operating leases do not give rise to property rights or lease obligations, and therefore the results of the lease agreements are not reflected in the Municipality's account groups.

The following is a schedule by years of future minimum rental payments under operating leases that have initial or remaining noncancelable lease terms in excess of one year as of June 30, 2009:

<u>Year Ending June 30,</u>	<u>Total</u>
2010	\$ 517,913
2011	517,913
2012	35,760
2013	35,760
2014	<u>35,760</u>
Total minimum payments required	<u>\$1,143,106</u>

12. COMPONENT UNIT

"Corporación Desarrollo Cultural Teatro Oliver, C.E."

Nature and Organization

"Corporación Desarrollo Cultural Teatro Oliver C.E." (non-profit organization) was organized under the laws of the Commonwealth of Puerto Rico. The Corporation was established to acquire "El Teatro Oliver of Arecibo" to be restored and operated as Municipal Theater.

Component unit financial statements of "Corporación Desarrollo Cultural Teatro Oliver C.E." were not available. As result, the component unit is not included as part of the Government-Wide Financial Statements.

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

13. PENSION PLAN

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

Members who have attained 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have completed ten years of creditable service are entitled to an annual benefit payable monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation, as defined, multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined; otherwise they will receive 75 percent of the average compensation, as defined. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$ 550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions during the year ended June 30, 2009 amounted to \$1,151,371. This amount represented 100% of the required contribution.

On September 24, 1999, an amendment to Act. No. 447 of May 15, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employee's participation in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 1, 2000, will only be allowed to become members of System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age.

The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee'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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

13. PENSION PLAN (CONTINUED)

Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2009, a copy of which can be obtained from the Retirement System, Minillas Station, PO Box 42003, San Juan, PR 00940.

14. RISK MANAGEMENT

The Property Division is responsible of assuring that the Municipality's property is properly insured. Annually, the Property Division compiles the information of all property owned and its respective market value. After evaluating this information, the Property Division submits the data regarding the Municipality's properties to the Area of Public Insurance Department at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities.

15. COMMITMENTS AND CONTINGENCIES

A. Claims and lawsuits:

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities.

With respect to pending and threatened litigation, the Municipality has reported liabilities of \$1,812,243 in the Government-Wide Financial Statements for awarded and anticipated unfavorable judgments.

The Municipality participates in a number of federal financial assistance programs funded by the Federal Government. Expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantor. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the Municipality management expects such amounts, if any, will not be material.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

16. FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

The GASB has issued the following statements that have effective dates after June 30, 2008:

- a. GASB Statement No.51, *Accounting and Financial Reporting for Intangible Assets*. This statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. This Statement is effective for periods beginning after June 15, 2009.
- b. GASB Statement No.53, *Accounting and Financial Reporting for Derivative Instruments*, which is effective for periods beginning after June 15, 2009.
- c. GASB Statement No.54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which is effective for periods beginning after June 15, 2010.
- d. GASB Concepts Statement No. 5, *Service Efforts and Accomplishments- an Amendment of GASB Concepts Statements No. 2*. This Statement provides a framework to be used by the GASB in considering guidance for reporting SEA by state and local governmental entities and amends terminology and other information in GASB:CS-2.

The impact of these statements on the Municipality's basic financial statements has not yet been determined.

17. SUBSEQUENT EVENTS

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

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

As part of this plan, the **Municipality of Arecibo** will benefit from federal grants to improve its services to its constituents and from the economic activity generated within its territory due to projects funded by ARRA. The Municipality expects funding to be awarded and expended in the following fiscal year 2009-2010.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)
YEAR ENDED JUNE 30, 2009**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u> (Budgetary Basis) (See Note 1)	<u>Variance with</u> <u>Final Budget</u> <u>Positive</u> <u>(Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Property taxes	\$ 11,210,047	\$ 11,210,047	\$ 11,372,444	\$ 162,397
Municipal license tax	14,853,000	14,853,000	13,509,878	(1,343,122)
Licenses, permits and other local taxes	1,360,000	1,360,000	931,800	(428,200)
Charges for service	721,000	721,000	62,313	(658,687)
Intergovernmental	9,882,544	9,882,544	8,674,486	(1,208,058)
Rent of property	489,536	489,536	551,744	62,208
Fines and forfeitures	65,000	65,000	236,993	171,993
Interest	1,998,293	1,998,293	507,438	(1,490,855)
Miscellaneous	350,000	350,000	2,041,700	1,691,700
Transfer in	<u>3,800,000</u>	<u>3,800,000</u>	<u>3,352,532</u>	<u>(447,468)</u>
Total revenues	<u>44,729,420</u>	<u>44,729,420</u>	<u>41,241,328</u>	<u>\$ (3,488,092)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER				
FINANCING USES:				
Current:				
General government	\$ 26,969,004	\$ 26,574,505	\$ 29,076,826	\$ (2,502,321)
Public safety	4,656,816	4,651,751	4,181,336	470,415
Public works	10,624,706	11,081,267	10,601,848	479,419
Culture and recreation	889,090	851,636	984,669	(133,033)
Operating transfer to other fund	<u>1,589,804</u>	<u>1,570,261</u>	<u>1,434,131</u>	<u>136,130</u>
Total expenditures, encumbrances and other financing uses	<u>\$ 44,729,420</u>	<u>\$ 44,729,420</u>	<u>\$ 46,278,810</u>	<u>\$ (1,549,390)</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)				
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (5,037,482)</u>	<u>\$ (5,037,482)</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis)"available for appropriation" from the budgetary comparison schedule				\$ 41,241,328
Differences-budget to USGAAP:				
Non-budgeted transfer in				1,072,642
USGAAP adjustments to revenues				<u>(54,607)</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 42,259,363</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$ 46,278,810
Differences-budget to USGAAP:				
Non-budgeted expenditures				(254,561)
Prior year encumbrances recorded as current year expenditures for USGAAP basis				2,283,273
Current year encumbrances recorded as expenditures for budgetary basis				<u>(1,056,308)</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 47,251,214</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

NOTES TO THE BUDGETARY COMPARISON SCHEDULE – GENERAL FUND

YEAR ENDED JUNE 30, 2009

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

a. Budgetary Control

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with USGAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the general fund.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For USGAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.

The unencumbered balance of any appropriation at the end of the fiscal year will lapse at the end of such fiscal year. Other appropriations, mainly capital project 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.

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2009 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2009.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2009

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF AGRICULTURE:			
Pass-through the Commonwealth of Puerto Rico Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	\$ 857,529
Total U.S. Department of Agriculture			<u>857,529</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Community Development Block Grants/Entitlement Grants	14.218		3,179,839
Direct Program:			
Urban Development Action Grant	14.221		14,450
Direct Program:			
Emergency Shelter Grants Program	14.231		148,310
Direct Program:			
HOME Investment Partnerships Program	14.239		871,404
Direct Program:			
Section 8 Housing Choice Voucher Program	14.871		<u>4,134,508</u>
Total U.S. Department of Housing and Urban Development			<u>8,348,511</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2009

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S DEPARTMENT OF JUSTICE:			
Pass-through the Commonwealth Office of the Governor (CFWM): Rural Domestic Violence and Child Victimization Enforcement Grant Program	16.589	Not Available	<u>66,492</u>
Total U.S. Department of Justice			<u>66,492</u>
U.S. DEPARTMENT OF EDUCATION			
Pass-through the Commonwealth of Puerto Rico Department of Education: Even Start State Educational Services	84.213	Not Applicable	<u>17,082</u>
Total U.S. Department of Education			<u>17,082</u>
U.S DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico Governor's Office (Elderly Office):			
Special Programs for Aging – Title III, Part B – Grant for Supportive Services and Senior Centers	93.044	Not Available	98,247

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2009

U.S DEPARTMENT OF HEALTH AND HUMAN SERVICES: (CONTINUED)

Special Programs for Aging – Title III, Part C – Nutrition Services	93.045	Not Available	293,260
National Family Caregiver Support - Title III, Part E	93.052	Not Available	22,748
Nutrition Services Incentives Program	93.053	Not Available	18,580
Pass-through the Commonwealth of Puerto Rico Administration for Children and Families (ACUDEN):			
Community Services Block Grant	93.569	Not Available	35,822
Child Care and Development Block Grant	93.575	Not Available	1,014,405
Head Start	93.600	Not Available	<u>7,983,442</u>
Total U.S. Department of Health and Human Services			<u>9,466,504</u>

U.S. DEPARTMENT OF HOMELAND SECURITY:

Pass-through the Commonwealth of Puerto Rico Emergency Management Agency:			
Homeland Security Grant Program	97.067	Not Available	<u>146,260</u>
Total U.S. Department of Homeland Security			<u>146,260</u>

TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 18,902,378</u>
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The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2009

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the **Municipality of Arecibo** and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the fund financial statements. 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*.

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue Fund Head Start, Special Revenue Fund – Other Federal Grants, and Other Governmental Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the fund financial statements and the expenditures in the Schedule of Expenditures of Federal Awards is as follows:

<u>Description</u>	<u>Special Revenue Fund Head Start</u>	<u>Special Revenue Fund Other Federal Grants</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Per Schedule of Expenditures of Federal Awards	\$ 8,555,439	\$ 5,976,706	\$ 4,370,233	\$ 18,902,378
Non federal programs expenditures	<u>235,724</u>	<u>23,413</u>	<u>432,017</u>	<u>691,154</u>
Total expenditures in the fund financial statements	<u>\$ 8,791,163</u>	<u>\$ 6,000,119</u>	<u>\$ 4,802,250</u>	<u>\$ 19,593,532</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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

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

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Arecibo
Arecibo, Puerto Rico**

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Arecibo, Puerto Rico**, as of and for the year ended June 30, 2009, which collectively comprise the **Municipality's** basic financial statements and have issued our report thereon dated December 29, 2009, which was unqualified. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects **Municipality of Arecibo's** ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of **Municipality of Arecibo's** financial statements that is more than inconsequential will not be prevented or detected by **Municipality of Arecibo's** internal control. Significant deficiencies are described in the accompanying schedule of findings and questioned costs as items **09-01** through **09-04**.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by **Municipality of Arecibo's** internal control.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, of the significant deficiencies in internal control over compliance described above, we consider items **09-02** and **09-03** to be a material weakness.

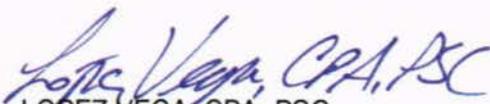
Compliance and Other Matters

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

We noted certain other matters that we reported to management of the **Municipality of Arecibo** in a separate letter dated December 29, 2009.

The **Municipality of Arecibo's** responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit **Municipality of Arecibo's** response and, accordingly, we express no opinion on it.

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


LOPEZVEGA, CPA, PSC

San Juan, Puerto Rico
December 29, 2009

Stamp No. 2407030 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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

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

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Arecibo
Arecibo, Puerto Rico**

Compliance

We have audited the compliance of the **Municipality of Arecibo** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. The **Municipality of Arecibo'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 of Arecibo's** management. Our responsibility is to express an opinion on the **Municipality of Arecibo's** compliance based on our audit.

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

In our opinion, the **Municipality of Arecibo** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which 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 as items, **09-05** through **09-11**.

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

Internal Control Over Compliance

The management of the **Municipality of Arecibo** is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the **Municipality of Arecibo's** internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of **Municipality of Arecibo's** internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies and others that we consider to be material weaknesses.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items **09-05** through **09-11** to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider items **09-05, 09-08, 09-09, 09-10** and **09-11** to be material weaknesses.

The **Municipality of Arecibo's** responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit **Municipality of Arecibo's** response and, accordingly, we express no opinion on it.



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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

We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Arcibo** in a separate letter dated March 10, 2010.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
March 10, 2010

Stamp No. 2407068 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2009

Section I – Summary of Auditor’s Results

Financial Statements

Type of auditor’s report issued: Unqualified, except for **adverse** for reporting entity.

Internal control over financial reporting:

Material weakness identified?	Yes	<input checked="" type="checkbox"/>	No
Significant deficiencies identified not considered to be material weaknesses?	Yes	<input checked="" type="checkbox"/>	None reported

Noncompliance material to financial statements noted?	Yes	No	<input checked="" type="checkbox"/>
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Federal awards

Internal Control over major programs:

Material weakness identified?	Yes	<input checked="" type="checkbox"/>	No
Significant deficiencies identified not considered to be material weaknesses?	Yes	<input checked="" type="checkbox"/>	None 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 Circular A-133, Section .510(a)?	Yes	<input checked="" type="checkbox"/>	No
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Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
10.558	Child and Adult Care Food Program
14.218	Community Development Block Grant
14.239	Home Investment Partnership Program
14.871	Section 8 Housing Choice Voucher
93.575	Child Care & Development Block Grant
93.600	Head Start Program

Dollar threshold used to distinguish between Type A and Type B programs	<u>\$567,071</u>
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Auditee qualified as low-risk auditee?	Yes	No	<input checked="" type="checkbox"/>
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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference **09-01**

Requirement **Financial Reporting – Accounting Records**

Statement of Condition During our examination of the Municipality's accounting system, we noted that it does not summarize the transactions in a formal General Ledger, in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal Funds). Also, the Municipality's accounting system did not provide its Governmental-Wide Financial Statements.

The Municipality did not include in the basic financial statements, audited financial information related to the "Corporación de Desarrollo Cultural Teatro Oliver".

Criteria Chapter VIII, Article 8.010 of State Act Number 81 of August 30, 1991, states that the Municipality should maintain an effective and updated accounting system.

GASB Statement No. 14 requires that the financial information of component units not be blended with similar financial information of the primary government. Rather, such information should be presented in the basic financial statements of the financial reporting entity.

Cause of Condition The Municipality did not maintain effective internal control over the transactions recorded on its accounting records. Also, the accounting data is not summarized in the form of a double-entry general ledger record.

The Municipality was unable to obtain audited financial statements of the "Corporación de Desarrollo Cultural Teatro Oliver", a Discrete Component Unit.

Effect of Condition The Municipality's accounting system did not provide updated and complete financial information that presents the financial position and the result of operations and the change in fund balances. Such information is necessary to take management decisions.

The Municipality is not in compliance with the *GASB Statement No. 14* requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference **09-01 (Continued)**

Recommendation We recommend that the Municipality should establish internal control and procedures in order to maintain an accounting system that contains information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, interfund transactions, etc.

Also, we recommend to the Municipality Management to require annual audited financial statements of the “Corporación de Desarrollo Cultural Teatro Oliver”, to the Component Unit management, to include them in the financial reporting entity basic financial statements.

Questioned Costs None

**Management Response
And Corrective Action**

The Municipality concurs with the finding. The Municipality maintains two set of accounting records; a manual system and a computerized system provided in the past by the Municipal Affairs Commissioner Office (OCAM). Actually, all of the transactions were recorded in both systems, but the manual system is the primary financial records for financial statements preparation purposes at the end of each fiscal year due to the fact that the computerized system real accounts balances carried forward from prior years were affected by accounting errors in the first years of the system operation.

Nevertheless, as part of the corrective action plan, the Commissioner of Municipal Affairs (“OCAM”) consider alternatives to improve the accounting system, including the acquisition of new accounting software, and therefore, we will hope to solve our accounting system condition in the near future. Although the Legislature of the Commonwealth of Puerto Rico has appropriated funds for the design and implementation of a new system, no further action has been taken on this matter.

The Municipality will meet the accountant from the “Corporación de Desarrollo Cultural Teatro Oliver” to discuss the manner in which the financial statements of the “Corporación” can be integrated to the financial statements of the Municipality.

Responsible Person: Mr. Guillermo Gabriel- Finance Director

Implementation date: July, 2010

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference **09-02**

Requirement **Cash Receipts – Revenue, Receivable - Collections**

Statement of Condition We performed a cash receipt test and examined a sample of thirty (30) collections. The following summarize the exceptions noted:

- a. In ten (10) cases, the Daily Receipts Validation Report was not available for examination and we could not trace the amounts collected to the deposit slip and bank statements.
- b. In twenty three (23) cases, the deposit slip was not available for our examination. This situation caused that the amounts tested could not be traced to the Daily Receipts Validation Report and we cannot verify if the collections were deposited in the correct bank account and accounted for in the correct fund and revenue account.
- c. In eighteen (18) cases, the treasurer did not include adequate evidential documentation (customer's remittance data as excise tax determination documents, and customer notification letters, etc.) which support the collections receipts CR01 and CR02.
- d. In five (5) taxpayer file's, the Municipal Tax License was not available for our examination.
- e. In one (1) taxpayer file's, the Audited Financial Statement was not available for our examination.

Criteria The Section Four (4) of the Chapter three (3) of the Revised Regulation on Basic Standards for Municipalities of Puerto Rico establishes that the Official Treasurer should realize a daily revision of amount collected and amounts credited in bank to assure that the revenues has been duly accounted and processed in the period of collection and in the correct fund.

Cause of Condition Internal control procedures failed to assure that daily collections are duly accounted for and duly recorded in the correct fund.

Effect of Condition In these cases the Municipality did not comply with regulations stated in The Section Four (4) of the Chapter three (3) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II - Financial Statements Findings

Finding Reference **09-02 (Continued)**

Recommendation The Municipality should establish adequate monitoring procedures to assure that collections are deposited in the correct bank account and accounted in the correct fund and revenue account. Also, an evaluation of office space and document control should be made to safeguard important documentation about daily transactions and taxpayer's files.

Questioned Costs None

**Management Response
And Corrective Action**

The Municipality concurs with the finding. The Municipality's Treasury Department will strengthen its monitoring procedures so that supporting documents are properly filed and available to provide to the auditors.

Responsible Person: Mr. Raymond Guzman - Director Treasury Department

Implementation Date: March, 2010

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference **09-03**

Requirement **Expenditures for Goods and Services and Accounts Payables-
Purchasing and receiving**

Statement of Condition We performed a cash disbursement test and examined twelve (12) disbursement vouchers which belonged to CDBG Program, thirteen (13) which belonged to HOME Program, four (4) which belonged to Child Care Development Grant, nine (9) which belonged to Child Care Food Program, thirty (30) which belong to Section 8 Housing Voucher Program, and twenty (20) which belong to Head Start Program. The following will summarize the internal control exceptions noted:

- a. In nine (9) cases, the Purchase Order was issued after the receiving of goods and services. (Seven (7) Purchase Orders corresponded to CDBG Program, and two (2) corresponded to Child Care Development Grant).
- b. In forty (40) cases, the Receiving Report and Inspection was not marked as paid. (Thirty six (36) Receiving Report corresponded to CDBG Program, and four (4) corresponded to Child Care Development Grant).
- c. In nineteen (19) cases, the Disbursement Voucher was not marked as paid. (Corresponded to Section 8 Housing Voucher Program).
- d. In twenty one (21) cases, the Purchase Order was not marked as paid. (Fifteen (15) corresponded to Section 8 Housing Voucher Program, three (3) corresponded to Child Care Development Grant and three (3) corresponded to CDBG Program).
- e. In ten (10) cases, the original invoice was not marked as paid. (Eight (8) corresponded to CDBG Program, and two (2) corresponded to Child Care Development Grant).
- f. In eleven (11) cases, the Disbursement Voucher was not available for our examination. (One (1) corresponded to CDBG Program, and ten (10) corresponded to Section 8 Housing Voucher Program).
- g. In fourteen (14) cases, the Purchase Order was not available for our examination. (All corresponded to Section 8 Housing Voucher Program).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference 09-03 (Continued)

- h. In five (5) cases, the Disbursement Voucher was not approved by pre interventor. (Four (4) corresponded to CDBG Program, and one (1) corresponded to Child Care Development Grant).
- i. In twenty two (22) cases, the Disbursement Voucher was not signed by the Official Payer. (One (1) corresponded to CDBG Program, one (1) corresponded to Child Care Development Grant, and twenty (20) corresponded to Section 8 Housing Voucher Program).
- j. In four (4) cases, the Disbursement Voucher and its justificants were not marked as paid. (Correspond to CDBG Program).
- k. In one (1) case, the Purchase Order was not signed by the Finance Director. (Corresponded to Section 8 Housing Voucher).
- l. In one (1) case, the Disbursement Voucher was not signed by the Finance Director. (Corresponded to Child Care Development Grant).
- m. In two (2) cases, the Requisition Sheet was not available for our examination. (Corresponded to Child Care Development Grant).
- n. In three (3) cases, the Disbursement Voucher was not signed by the Mayor or his Authorized Representative. (Two (2) corresponded to CDBG Program, and one (1) corresponded to Child Care Development Grant).
- o. In one (1) case, the Requisition Sheet was not signed by the Accounting Director or his Authorized Representative. (Corresponded to CDBG Program)

Criteria

The Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establish in the Chapter Four (4) that the Finance Director will be responsible to account and prepare disbursements through documents duly prepared and certified.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference **09-03 (Continued)**

Cause of Condition The Municipality internal control failed to assure that all documents supporting disbursement of funds are approved before disbursement of funds.

Effect of Condition The Municipality is not in compliance with Chapter Four (4) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.

Recommendation We recommend that the Municipality should improve its internal control and procedures in order to assure that disbursement vouchers, cancelled checks and other supporting documents are available for examination by auditors and includes all required documentation and approvals.

Questioned Costs None

Management Response

And Corrective Action The Municipality concurs with the finding. The Municipality will give specific instructions to each department and to the pre-interventor office that no disbursement will be made unless it complies with minimal documentation and supporting evidence, including all approvals.

Responsible Person: Mr. Guillermo Gabriel, Director Finance Department

Implementation date: March, 2010

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference	09-04
Requirement	Payroll and Related Liabilities – Personnel, Employment and Rate Authorizations
Statement of Condition	<p>We performed a payroll test and examined a sample of thirty (30) personnel files, and the related payroll documents of those functionaries and employees. The following will summarize the situations found:</p> <p>a. The Municipality has not established a Reclassification and Retribution Plan for regular employees. Also, the plan for functionaries and department directors has not been updated since 1985.</p>
Criteria	<p>Chapter XI Article 11.001 of State Act Number 81 of August 30, 1991 states that each Municipality's should establish an updated Reclassification and Retribution Plan for functionaries and regular employees. Article 11.006 states that all positions are subjected to Reclassification and Retribution Plan, adjusted to circumstances and necessities of the Municipality. The Mayor will establish the plan with the approval of the Municipal Legislature.</p>
Cause of Condition	<p>The Municipality's control and procedures failed to assure that the Municipality establishes a Reclassification and Retribution Plan for regular employees. Also, should update the plan for functionaries and department directors.</p>
Effect of Condition	<p>The Municipality is not in compliance with the Articles 11.001 (b) and 11.006 of State Act Number 81 of August 30, 1991.</p>
Recommendation	<p>We recommend that the Municipality should implement the necessary internal controls and procedures in order to comply with the requirements established in the State Act Number 81 of August 30, 1991.</p>
Questioned Cost	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II - Financial Statements Findings

Finding Reference **09-04 (Continued)**

**Management Response
and Corrective Action**

The Auditor's recommendation would be considered as part of corrective action plan development and implementation. Also, the Municipality will communicate with "ORHELA" for technical support in the implementation of the plan. We expect that the first phase will be implemented in the fiscal year 2010-2011.

Responsible Person: Mrs. Zoadme Rodríguez Aguila- Director of
Human Resources and Human Capital

Implementation Date: July 2011

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference **09-05**

Program **Community Development Block Grant/Entitlement Grants (CFDA 14.218); U.S. Department of Housing and Urban Development**

Requirement **Allowable Cost and Cost Principles**

Statement of Condition **Section II – Financial Statements Findings- Finding Reference 09-03.**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Federal Award Findings and Questioned Costs

Finding Reference	09-06
Program	Community Development Block Grant/Entitlement Grants (CFDA 14.218); U.S. Department of Housing and Urban Development
Requirement	Report – Performance Reporting
Statement of Condition	HUD-60002, <i>Section 3 Summary Report, Economic Opportunities for Low and Very Low-Income Persons</i> , (OMB No. 2529-0043) was not submitted for the fiscal year ended June 30, 2009.
Criteria	24 CFR Sections 135.3 (a), 135.90, and 570.607. Section 135.3 (a) states that Section 3 applies to training, employment, contracting and other economic opportunities arising in connection with the expenditure of housing assistance and community development assistance that is used for the following projects: Housing rehabilitation, housing construction, and other public construction. Section 135.90, states that each recipient which receives directly from HUD financial assistance that is subject to the requirements of this part shall submit an annual report for the purpose of determining the effectiveness of Section 3. Where the program providing the Section 3 assistance requires submission of an annual performance report, the Section 3 report will be submitted with the annual performance report. If the program does not require an annual performance report the report shall be submitted by January 10 of each year or within 10 days of project completion, whichever is earlier. Section 570.607 states regulations for employment and contracting opportunities for low and very low income persons.
Cause of Condition	The Municipality did not comply with the established regulation as prescribed by HUD.
Effect of Condition	The Municipality could lose federal programs funds for the noncompliance with HUD requirements stated in 24 CFR 135.3 (a), 135.90, and 570.607.
Recommendation	Procedures should be implemented to ascertain that the Municipality complies with the established Federal Regulation, as prescribed by HUD.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Federal Award Findings and Questioned Costs

Finding Reference **09-07**

Program **Home Investment Partnership Program (CFDA. No. 14.239); U.S. Department of Housing and Urban Development**

Requirement **Period of Availability of Funds**

Statement of Condition During our audit we proceeded to examine the Summary of Consolidated Plan Projects for report year 2008 (C04PR06) as of June 30, 2009 obtained from the IDIS System and compare it to the Home program general ledger. After our procedures were performed we noted that the IDIS System report details the following available balances to draw as follows:

Activity	Program year	Amount available to draw
Planning and Administrative	1997	\$6,149
Planning and Administrative	2001	1,664
Planning and Administrative	2002	1,533
Planning and Administrative	2003	2,009
Planning and Administrative	2004	6,068
CHDOS	2001	102,450

Also, we found that for CHDOS grants 2002, 2004 & 2006, there are differences in the amounts reported in C04PR06 against the amounts in COPR25.

Criteria 24 CFR, Section 92.204-2 (a) and (b) states that funds has to be committed within twenty four months after the last day of the month in which HUD notifies the entity of HUD's execution of the HOME agreement. Also, the funds have to be expended within five years after the last day of the month in which HUD notifies the entity of HUD's execution of the agreement.

Cause of Condition The Municipality did not maintain adequate controls to assure that the funds are committed and expended at the required period.

Effect of Condition The Municipality is not in compliance with 24 CFR, Section 92.204-2 (a) and (b).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Federal Award Findings and Questioned Costs

Finding Reference **09-07 (Continued)**

Recommendation The Municipality should establish adequate procedures to assure that accounting records balances to commit are in line with the IDIS System in order to correct the differences and to assure that funds are committed and expended in the required period.

Questioned Costs None

Management Response The Municipality Management concurs with the finding. The Program Coordinator will review the fund balances with the accounting office of the Municipal Development Department so that those funds are used promptly and within programs' regulations. The program started to disburse the amounts corresponding to CHDOS during the fiscal year 2009-2010. Also, the program will review its processes to assure that all IDIS system data output, agrees with accounting records.

Responsible Person: Sandra Ayala- Program Coordinator

Implementation date: March, 2010

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference **09-08**

Program **Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S.
Department of Housing and Urban Development**

Requirement **Allowable Cost and Cost Principles**

Statement of Condition **Section II – Financial Statements Findings- Finding Reference 09-03.**

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III - Mayor Federal Award Program Findings and Questioned Costs

Finding Reference 09-09

Program Child Care and Development Block Grant (CFDA. No. 93.575); U.S. Department of Health and Human Services; Pass through State - Commonwealth of Puerto Rico Administration for Children and Families.

Requirement Allowable Cost and Cost Principles

Statement of Condition **Section II** - Financial Statements Findings- Finding Reference 09-03.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference	09-10
Program	Child Care and Development Block Grant (CFDA. No. 93.575); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico Administration for Children and Families.
Requirement	Cash Management
Statement of Condition	We realized Cash Management Test and we found the following exceptions: a. The program funds were not disbursed on a reasonable lapse of time after the transfer of funds. b. During six (6) months the cash as per bank reconciliation was in overdraft.
Criteria	CFR 45, Subpart C, Section 92.20 (b) (7), requires a cash management system in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursements made by the grantee.
Cause of Condition	The procedures established by ACUDEN in the delegation of funds agreement do not provide a clause to comply with this requirement.
Effect of Condition	The Municipality is not in compliance with 45 CFR, Subpart C, Section 92.20 (b) (7).
Recommendation	We recommend management to require ACUDEN alternate methods to request cash in order to comply with this requirement.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference **09- 10 (Continued)**

Management Response

And corrective action The Municipality management agrees with the finding. The Program Coordinator will make a written request to “ACUDEN” for advice regarding this finding.

Responsible Person: Ivette Nazario– Program Accountant

Implementation date: July, 2010

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference	09-11
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico Administration for Children and Families
Requirement	Cash Management
Statement of Condition	We realized Cash Management Test and we found the following exceptions: <ul style="list-style-type: none">a. The program requested funds that were not disbursed on a reasonable lapse of time.b. During ten (10) months the cash as per bank reconciliation was in overdraft.
Criteria	CFR 45, Subpart C, Section 92.20 (b) (7), requires a cash management system in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursements made by the grantee.
Cause of Condition	The procedures established by ACUDEN in the agreement of delegation of funds do not provide a clause to comply with this requirement.
Effect of Condition	The Municipality is not in compliance with 45 CFR, Subpart C, Section 92.20 (b) (7).
Recommendation	We recommend management to require ACUDEN alternate methods to request cash in order to comply with this requirement.
Questioned Costs	None
Management Response And Corrective Action	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

Responsible Person: Mrs. María Torres – Program Accountant

Implementation date : March,2010

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2009

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
08-05	14.218	<p><u>Management should implement procedures to ascertain that the Municipality complies with the established Federal Regulation, as prescribed by HUD.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 09-06.</p>
08-06	14.871	<p><u>Management should improve its internal control and procedures in order to assure that disbursement vouchers, cancelled checks and other supporting documents are available for examination by auditors and includes all required documentation and approvals.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 09-08.</p>
08-07	93.575	<p><u>Management should require ACUDEN alternate methods to request cash in order to comply with this requirement.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 09-10.</p>
08-08	93.575	<p><u>Management should follow monitoring system procedures developed, including informing contractors in the procurement process and prior to contractual agreement signature about the applicability of Davis Bacon Act, through field visits, realize contractors and subcontractors interviews, obtaining contractor's and subcontractor's weekly payrolls to be reviewed on a weekly basis to establish the degree of compliance and the nature and extend of violations, if any, and then, communicate contractors promptly about any failure in the payroll process.</u></p> <p>Corrective action was taken.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARECIBO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
08-09	93.600	<p><u>Management should require ACUDEN alternate methods to request cash in order to comply with this requirement.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 09-11.</p>
07-10	93.575	<p><u>Management should require ACUDEN alternate methods to request cash in order to comply with this requirement.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 09-10.</p>
07-11	93.600	<p><u>Management should require ACUDEN alternate methods to request cash in order to comply with this requirement.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 09-11.</p>
06-05	93.575	<p><u>Management should require ACUDEN alternate methods to request cash in order to comply with this requirement.</u></p> <p>Audit finding is no longer valid since has passed more than two (2) years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow-up to the finding and has not issued a final decision respect to the finding.</p>
06-06	93.600	<p><u>Management should require ACUDEN alternate methods to request cash in order to comply with this requirement.</u></p> <p>Audit finding is no longer valid since has passed more than two (2) years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow-up to the finding and has not issued a final decision respect to the finding.</p>