

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

**MUNICIPIO DE ARECIBO
AUDITORÍA 2012-2013
30 DE JUNIO DE 2013**

Commonwealth of Puerto Rico
Autonomous Municipality of Arecibo

**BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION**

Fiscal Year Ended June 30, 2013

(With the Additional Reports and Information Required by
the Government Auditing Standards and OMB Circular A-133)



CPA DIAZ-MARTINEZ, PSC

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

AICPA Governmental
Audit Quality Center

Member of: American Institute of Certified Public Accountants (AICPA)
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PART I
FINANCIAL

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INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of **Autonomous Municipality of Arecibo of the Commonwealth of Puerto Rico (Municipality)**, as of and for the fiscal year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise **Municipality's** basic financial statements as listed in the Table of Contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 *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 financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the **Municipality's** preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that our audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

INDEPENDENT AUDITOR'S REPORT
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Autonomous Municipality of Arecibo
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Basis for Qualified Opinion on Governmental Activities

During our audit the **Municipality** did not provide a subsidiary of capital assets that agreed with the amounts reported in governmental activities of the Governmental-Wide Financial Statements and, accordingly, the depreciation expense on those assets is not supported. Accounting principles generally accepted in the United States of America require that those capital assets been supported to present the assets, net position, and expense of the governmental activities. The amount by which this departure would affect the assets, net position, and expenses of the governmental activities has not been determined.

Qualified Opinion

In our opinion, except for the effects of the matters discussed in the "Basis for Qualified Opinion" paragraph, the financial statements referred to above present fairly, in all material respect, the respective financial position of the governmental activities of the **Autonomous Municipality of Arecibo of the Commonwealth of Puerto Rico**, as of June 30, 2013, and the respective changes in financial position thereof for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Unmodified Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the **Autonomous Municipality of Arecibo of the Commonwealth of Puerto Rico**, as of June 30, 2013, and the respective changes in financial position thereof for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matter

Newly Adopted Standards

As discussed in Note 23 to the financial statements, the **Municipality** adopted new accounting guidance, Governmental Accounting Standards Board (GASB) Statement No. 61, *The Financial Reporting Entity: Omnibus an Amendment of GASB Statements No. 14 and No. 34*, GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, GASB Statement No. 64 *Derivative Instruments: Application of Hedge Accounting Termination Provisions – an amendment of GASB Statement No. 53*, and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* effective July 1, 2012. Our opinions is not modified with respect to this matter.

Other Matters

Restatement of Prior Year Financial Statements

As discussed in Note 22 to the financial statements, the 2012 financial statements have been restated to correct misstatements. Our opinions is not modified with respect to this matter.



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Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 6 through 18, and budgetary comparison information on pages 60 and 61 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the **Municipality's** basic financial statements. The accompanying Financial Data Schedule – Section 8 Housing Choice Vouchers Program, as required by U.S. Department of Housing and Urban Development, on pages 63 through 65, and the Schedule of Expenditures of Federal Awards, as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organization*, on pages 67 through 69, are presented for purposes of additional analysis and are not required parts of the basic financial statements.

The accompanying Financial Data Schedule – Section 8 Housing Choice Vouchers Program and the Schedule of Expenditures of Federal Awards are the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Financial Data Schedule – Section 8 Housing Choice Vouchers Program and the Schedule of Expenditures of Federal Awards are fairly stated, in all material respects, in relation to the financial statements as a whole.



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Other Reporting Required by *Governmental Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated July 30, 2014 on our consideration of the **Municipality's** internal control over financial reporting on our test 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* in considered **Municipality's** internal control over financial reporting and compliance.



CPA Díaz-Martínez, PSC
Certified Public Accountants & Consultants
License Number 12, expires on December 1, 2016

Caguas, Puerto Rico
July 30, 2014

Stamp No. E100093 was affixed to
the original report.



COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

This discussion and analysis of the Autonomous Municipality of Arecibo (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2013. 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, 2012. 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 2013 deserve special mention:

1. The Municipality Government-Wide Financial Statements reported total assets of \$151,333,232, total liabilities of \$107,918,796, and a Net Position of \$43,414,436.
2. The Municipality net position decreased by \$4,846,665 or 10%, basically due to an increase in claims and judgments of \$5,065,424.
3. As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$6,519,734, a reduction of \$3,606,448 or 36% due to excess expenditures over revenues and other financial sources.
4. In the fund financial statements, the governmental activities revenues increased \$1,409,687 or 1.08% while governmental activities expenditures decreased \$11,571,778 or 8% in comparison with prior year.
5. The general fund (the primary operating fund) reflected, on a current financial resource basis, a reduction of \$1,864,969 or 14% due to excess expenditures over revenues and other financing sources.
6. As the end of the current fiscal year the Municipality's General Fund deficit amounted to \$15,841,401, compared to a deficit of \$13,976,432 (as restated – see Note 22) in the prior fiscal year.
7. On a budgetary basis, actual expenditures exceeded actual revenues by \$2,593,903, caused due to unfavorable variances in revenues accounts of \$6,686,745 and a favorable variance in expenditures accounts of \$4,092,842.

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

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 2013. 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 basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. The basic financial statements include two types of statements that present unique views of the Municipality's financial position. This report also contains required supplementary information (budgetary schedule).

Government-Wide Financial Statements

The government-wide financial statements are intended to provide readers with a broad overview of the Municipality's financial position. They are presented using accounting methods very similar to a privately owned business, or the economic resources measurement focus, and full accrual accounting.

- a. The Statement of Net Position present information on all of the Municipality's assets, deferred outflows of resources, liabilities and deferred inflows of resources, with the balance between the two reported as Net Position. Over time, increases or decreases in net position can serve as an indicator of the Municipality's financial condition.
- b. The Statement of Activities presents information showing how the Municipality's net position changed during the given fiscal year. In this statement all changes in net position are reported as soon as the underlying event giving rise to the change occurs regardless of when cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will only affect cash flows in future fiscal periods.

The government-wide financial statements distinguish functions of the Municipality that are principally supported by Taxes, Capital Grants and Contributions (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges. The governmental activities of the Municipality include general government, public safety, public works, culture and recreation, health and welfare, urban development, claims and losses, education, training and employment, special communities, projects, depreciation and principal plus interest on related long-term debt.

The reader will need to consider non-financial factors, such as changes in the Municipality's property tax base and the condition of the roads, to assess the overall health of the Municipality.

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

The government-wide financial statements can be found on pages 19 to 20 of this report.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Accordingly, the governmental funds use the modified accrual basis of accounting. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements.

The Municipality maintains five (5) individual governmental funds: General Fund, Head Start Fund, Capital Activities Fund, Debt Service Fund and Other Governmental Funds. Information is shown in the balance sheet and in the statement of revenues, expenditures and changes fund balances.

Because the focus of governmental funds is narrower than that of the government wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the Municipality's near term financial decisions. The Governmental fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balance (Deficit) provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The governmental funds financial statements can be found on pages 21 through 24 of this report.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the basic financial statements can be found on pages 25 through 58 of this report.

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information. This section includes a budgetary comparison schedule, which includes reconciliation between the statutory fund balance for budgetary purposes and the fund balance for the General Fund as presented in the governmental fund financial statements.

The budgetary comparison schedule can be found on the pages 60 and 61 of this report.

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. Governmental Accounting Standard Board ("GASB 34") requires that these assets be valued and reported in the Government-Wide Statement of Net Position.

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

According to the requirements of GASB 34, the government must elect to either (a) depreciate the aforementioned assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery to near perpetuity. If the government develops the asset management system, (the modified approach) which periodically (at least every three years), by category, measures and demonstrate its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation.

In this particular respect, the Municipality has elected the use of recognizing depreciation under the useful life method and it contemplates to continue this treatment on said basis.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Government-wide Financial Analysis

Assets

As of June 30, 2013, the Municipality's total assets amounted to \$151,333,232, a reduction of \$2,478,158 or 2% when compared with \$153,811,390 (as restated – see Note 22) in the prior year. The assets exceeded its liabilities by \$43,414,436.

Capital assets net of depreciation – \$125,250,123 – include items such as infrastructure, buildings, equipment, machinery, land and other tangible items. Infrastructures include streets, sidewalks, bridges, and others. The Municipality uses capital assets to provide services to the community and thus they are not available for immediate spending. Total capital projects still in process amount to \$5,059,938. During the current fiscal year the Municipality's net capital assets decreased by \$642,013 or 0.1 percent.

Any resources needed to repay the debt associated with capital assets must be provided from sources other than the capital assets themselves since the capital assets cannot be liquidated to pay the related liabilities.

Liabilities

At the end of fiscal year 2013, total liabilities amounted to \$107,918,796. The current liabilities decreased by \$599,383 and at the end of the current fiscal year, the Municipality had outstanding long term debt (bonds, notes and other) of \$93,269,558. During the current fiscal year, the Municipality's issued new long-term liabilities in the amount of \$505,000. For more details see also page 46 and Note 11 – Non-Current Liabilities.

Net Position

The Statement of Net Position serves as an important indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Autonomous Municipality of Arecibo, assets exceed total liabilities by \$43,414,436 at the end of 2013, as compared to \$48,762,101 (as restated – see Note 22) in prior fiscal year. The following condensed Statement of Net Position shows on a comparative basis the most important components of the \$4,846,665 or 10% decrease reflected in the Net Position figure.

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

**Condensed Statement of Net Position
As of June 30, 2013 and 2012**

	<u>2013</u>	<u>RESTATED 2012</u>	<u>Change</u>	<u>%</u>
ASSETS				
Current and other assets	\$ 26,083,109	\$ 27,919,254	\$ (1,836,145)	-7%
Capital assets	<u>125,250,123</u>	<u>125,892,136</u>	<u>(642,013)</u>	-1%
Total assets	<u>151,333,232</u>	<u>153,811,390</u>	<u>(2,478,158)</u>	-2%
LIABILITIES				
Current and other liabilities	14,649,238	15,248,621	(599,383)	-4%
Long-term debt	<u>93,269,558</u>	<u>90,301,668</u>	<u>2,967,890</u>	3%
Total liabilities	<u>107,918,796</u>	<u>105,550,289</u>	<u>2,368,507</u>	2%
NET POSITION				
Net Investment in Capital Assets	85,120,257	94,197,136	(9,076,879)	-10%
Restricted	19,958,781	28,599,882	(8,641,101)	-30%
Unrestricted (Deficit)	<u>(61,664,602)</u>	<u>(74,535,917)</u>	<u>12,871,315</u>	-17%
Total net position	<u>\$ 43,414,436</u>	<u>\$ 48,261,101</u>	<u>\$ (4,846,665)</u>	-10%

The net position consist of the excess of assets over related liabilities. The negative –portion of net position are the consequence of previous budgets which did not provide funding for incurred long-term obligations, such as compensated absences, claims and judgments and others. Historically, such obligations have been budgeted, as the Municipality pays, without providing funding for their future liquidation.

An additional portion of the Municipality's net position represents the investment in capital assets, such as land, building, equipment, among others, less any outstanding related debt used to acquire those assets. The Municipality uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although, the Municipality's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from Debt Service Fund, since the capital assets themselves cannot be used to liquidate these liabilities. The amounts restricted for debt service and for other purposes, represent another portion of the net position, and these are resources subject to external restrictions.

Changes in Net Position

The Municipality's net position decreased by \$4,846,665, due to excess expenses over revenues. Approximately 42% of the Municipality's total revenue came from taxes, while 56% resulted from grants and contributions, including federal aid. Charges for Services provided 1%, Interest and others 1% of total revenues. The Municipality's largest expenses included items such as general government, public instruction, human services and welfare, culture and recreation, health and sanitation, public services and public works. The following statement of activities includes the composition of revenues and expenses for the fiscal years ended on June 30, 2013 and 2012 (as restated – see Note 22).

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

Statement of Activities
For the fiscal year ended June 30, 2013 and 2012

	<u>2013</u>	<u>RESTATED</u> <u>2012</u>	<u>Change</u>	<u>%</u>
Program revenues				
Charge for services	\$ 777,794	\$ 201,105	\$ 576,689	287%
Operating grants and contributions	21,498,285	19,680,517	1,817,768	9%
Capital grants and contributions	-	2,700,224	(2,700,224)	100%
General revenue				
Property taxes	16,168,931	16,946,562	(777,631)	-5%
Municipal taxes	6,286,528	7,523,123	(1,236,595)	-16%
Municipal sales and use tax	4,406,374	3,864,768	541,606	14%
Grants and contributions unrestricted	15,245,792	10,479,307	4,766,485	45%
Other taxes	1,080,286	1,255,238	(174,952)	-14%
Net gain on sale of capital asset	-	436,423	(436,423)	-100%
Miscellaneous	<u>513,778</u>	<u>1,480,814</u>	<u>(967,036)</u>	-65%
Total revenues	<u>65,977,768</u>	<u>64,568,081</u>	<u>1,409,687</u>	2%
Expenses				
General government	32,038,854	40,001,429	(7,962,575)	-20%
Public safety	4,260,765	4,611,570	(350,805)	-8%
Public works	4,153,575	8,452,043	(4,298,468)	-51%
Health and sanitation	9,088,297	8,556,684	531,613	6%
Culture and recreation	2,696,093	3,992,538	(1,296,445)	-32%
Economic development	-	217	(217)	-100%
Community and urban development	2,478,557	3,028,461	(549,904)	-18%
Education	13,287,448	11,327,777	1,959,671	17%
Interest	<u>2,820,844</u>	<u>2,926,492</u>	<u>(105,648)</u>	-4%
Total expenses	<u>70,824,433</u>	<u>82,897,211</u>	<u>(12,072,778)</u>	-15%
Change in net position	(4,846,665)	(18,329,130)	13,482,465	-74%
Net position beginning of year	<u>48,261,101</u>	<u>66,590,231</u>	<u>(18,329,130)</u>	
Net position end of year	<u>\$43,414,436</u>	<u>\$48,261,101</u>	<u>\$ (4,846,665)</u>	

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

Governmental Funds

The focus of the Municipality's governmental funds is to provide information on short-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.

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

Combined Fund Balances

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$6,519,734, a decrease of \$3,606,448 or 36% in comparison with the prior year of \$10,126,182 (as restated – see Note 22). The combined fund balances include restricted fund balances amounting to \$23,098,213. This is the portion of fund balance that reflects resources that are subject to externally enforceable legal restriction 1) to pay for specific program purposes (\$2.2 million); 2) to pay for capital projects (\$16.0 million) and 3) to pay for debt services (\$5.0 million). There are committed fund balances amounting to \$14,526 that can only be used pursuant to constraint formally imposed by the Municipal Legislature, by ordinances and resolutions. Consequently, since there is an excess of restricted and committed fund balances over total fund balances, a negative unassigned fund balance (or deficit) of \$16,593,005 was reported in the governmental funds at June 30, 2013.

Analysis of Financial Position of Governmental Funds

**Condensed Balance Sheet - Governmental Funds
For the fiscal year ended June 30, 2013 and 2012**

	<u>2013</u>	<u>RESTATED 2012</u>	<u>Change</u>	<u>%</u>
ASSETS				
Total assets	<u>\$36,242,549</u>	<u>\$34,108,785</u>	<u>\$ 2,133,764</u>	6%
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES				
Total liabilities	<u>29,722,815</u>	<u>23,982,603</u>	<u>5,740,212</u>	24%
FUND BALANCE				
Restricted	23,098,213	24,832,459	(1,734,246)	5%
Committed	14,526	8,959	5,567	-99%
Unassigned (deficit)	<u>(16,593,005)</u>	<u>(14,715,236)</u>	<u>(1,877,769)</u>	19%
Total fund balance	<u>\$ 6,519,734</u>	<u>\$10,126,182</u>	<u>\$ (3,606,448)</u>	-36%

As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$6,519,734, a reduction of \$3,606,448 or 36% due to excess expenditures over revenues and other financial sources.

Major Governmental Funds

General Fund (GF) – The GF is the principal operating fund of the Municipality. The GF's total assets amounted to \$6,212,092 at June 30, 2013. Such assets consist of: (1) Cash \$4,424,282, (2) cash with fiscal agent \$153,968 (3) taxes receivable \$526,010, (4) receivable from intergovernmental grants and contributions \$632,510, (5) due from other funds \$475,322.

The GF's total liabilities and deferred inflow of resources amounted to \$22,053,493 at June 30, 2013. Such liabilities are composed of: (1) account payable and accrued liabilities \$3,580,782, (2) intergovernmental payables \$3,033,303, (3) unearned revenues \$5,702,652 (4) due to other funds \$9,114,398, and (5) deferred inflow of resources \$622,358.

continue

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

At the end of the current fiscal year, the GF reported a fund deficit of \$15,841,401 compared to a deficit of \$13,976,432 (as restated – see note 22) in the prior fiscal year; reporting, on a current financial resource basis, a reduction of \$1,864,969 or 14% due to excess expenditures over revenues and other financing sources.

Head Start Fund (HSF) – The HSF's total assets amounted to \$810,021 at June 30, 2013, which consist mainly of restricted cash \$412, due from Grantor \$416,429, and due from other funds \$393,180. The HSF's total liabilities amounted to \$810,021 at June 30, 2013. Such liabilities are composed of: (1) account payable and accrued liabilities \$186,311, due to other funds \$483,000, and (2) deferred revenues \$140,710. At the end of the current fiscal year and for prior fiscal year, HSF's reported no fund balance.

Capital Activities Fund (CAF) – The CAF's total assets amounted to \$16,579,751 at June 30, 2013, which consist mainly of (1) restricted cash \$7,438,813, (2) due from other funds \$9,140,938. At the end of the current fiscal year, CAF's reported accounts payable of \$508,248, and total reserved fund balance reached \$16,071,503 compared to \$17,338,395 (as restated – see note 22) in the prior fiscal year, for a decrease of 1,266,892 or 7%.

Debt Services Fund (DSF) – The DSF's total assets amounted to \$10,423,396 at June 30, 2013, which consist of restricted cash in fiscal agent \$9,854,519 and taxes receivable of \$568,877. The DSF's total liabilities amounted to \$4,898,487 at June 30, 2013, which are composed of: (1) matured bonds due and payable \$3,706,000, and (2) interest payable \$1,192,487. At the end of the current fiscal year, DSF's total reserved fund balance reached \$4,956,032 compared to \$5,445,240 (as restated – see note 22) in the prior fiscal year, for a decrease of 489,208 or 9%.

Analysis of Operating Results of Governmental Funds

**Condensed Statement of Revenues, Expenditures and changes
In Fund Balance – Governmental Funds
Fiscal Years Ended June 30, 2013 and 2012**

	<u>2013</u>	RESTATED <u>2012</u>	<u>Change</u>	<u>%</u>
Revenues				
Total revenues	\$65,171,177	\$64,947,336	\$ 223,841	0%
Expenditures				
Total expenditures	<u>69,282,625</u>	<u>86,525,872</u>	<u>(17,243,247)</u>	-20%
Excess (deficiency) Revenues over expenditures	(4,111,448)	(21,578,536)	17,467,088	-81%
Other financing sources (uses) net	<u>505,000</u>	<u>7,840,000</u>	<u>(7,335,000)</u>	-94%
Changes in fund balance - net	(3,606,448)	(13,738,536)	10,132,088	-74%
Fund Balance beginning of year	<u>10,126,182</u>	<u>23,864,718</u>	<u>(13,738,536)</u>	
Fund Balance end of year	<u>\$ 6,519,734</u>	<u>\$10,126,182</u>	<u>\$ (3,606,448)</u>	

continue

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$6,519,734, a reduction of \$3,606,448 or 36% due to excess expenditures over revenues and other financial sources.

In the fund financial statements, the governmental activities revenues increased \$223,841 or 0.3% while governmental activities expenditures decreased \$17,243,247 or 20% in comparison with prior year.

Major Governmental Funds

General Fund (GF) - The total fund balance of the GF decreased by \$1,864,969 or 14% during current fiscal year, due to excess expenditures over revenues and other financing sources.

The GF reported total revenues of \$38,038,028. Approximately 57% (\$21,379,792) of the GF's total revenues for the current fiscal year came from property taxes, municipal license, construction excise taxes and sales and use taxes, while 40% (\$15,288,380) resulted from intergovernmental grants and contributions, charges for services provide 1% (\$455,716), and miscellaneous revenues 2% (\$914,140).

The GF reported total expenses of \$39,688,795. The largest expenses of the GF for the fiscal year ended June 30, 2013 were related to: (1) general administrative and operating costs \$26,492,225, which were classified as "General government; and Mayor and Municipal Legislature", (2) public works \$3,013,597, (3) public safety \$4,009,196, (4) health, sanitation and solid waste disposal \$2,090,523, (5) culture and recreation \$1,742,882, and (6) public instruction \$1,982,547.

Other financing uses (\$214,202) were net transfers to other funds of \$719,202, less an operational loan proceed of \$505,000.

Head Start Fund (HSF) - Total revenue of HSF's for the current fiscal year came from Federal Grant \$11,299,462. HSF's total expenditures for the current fiscal year were used for public instruction services \$11,299,462. No change in fund balance was reported for the current fiscal year.

Capital Activities Funds (CAF) - The CAF's total fund balance decreased by \$1,266,893 or 7% during current fiscal year. Total revenue of CAF's for the current fiscal year came from Local and Federal Governments Grants \$955,350. CAF's total expenditures for the current fiscal year were mainly used for capital outlays \$1,624,658 and urban development \$428,375. Other financing uses were net transfers to other funds (\$169,062).

Debt Services Fund (DSF) - The total fund balance of the DSF's decreased by \$489,208 or 9% during current fiscal year. Property taxes provided \$4,737,601 (83%) of DSF's total revenues, and Sales and use taxes \$992,449 (17%) for a total revenue of \$5,730,050 in the current fiscal year. DSF's total expenditures for the current fiscal year were related to payment of principal and interests \$7,193,258. Other financing sources amounted to \$974,000, in net transfers from other funds.

GENERAL FUND BUDGETARY HIGHLIGHTS

For fiscal year 2012-2013, the Municipal Legislature approved an original budget for the General Fund of \$44,724,773. During the year, there was an amendment to include an operational loan of \$505,000 obtained during the course of the fiscal year for a final approved budget of \$45,229,773. The budgetary comparison reflected a deficiency of \$2,593,903 due to actual amount of charges to appropriations (budgetary basis) of \$41,136,931 with a favorable variance of \$4,092,842 or 9% under an unfavorable variance of \$6,686,745 or 15% in actual amounts of resources (budgetary basis) of \$38,543,028.

continue

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2013, amounted to \$174,219,369, which upon deduction of accumulated depreciation in the amount of \$48,969,246; produce a net book value attributable to capital assets in the amount of \$125,250,123. This investment 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. The net decrease of \$642,013 in the Municipality's investment in capital assets for the current fiscal year represented approximately 0.5 percent of net book value. Depreciation charges for the year totaled \$3,652,648.

The following chart summarizes the Municipality's capital assets for the fiscal years ended June 30, 2013 and 2012.

CAPITAL ASSETS		
(Net of accumulated depreciation)		
	<u>2013</u>	<u>2012</u> <u>RESTATED</u>
Land	\$ 57,595,654	\$ 57,595,654
Work of arts	157,261	157,261
Construction in progress	5,059,938	10,314,043
Building and building improvements	43,828,699	42,429,632
Infrastructure and infrastructure improvements	16,426,237	12,522,437
Machinery and equipment	<u>2,182,334</u>	<u>2,873,109</u>
TOTAL	<u>\$125,250,123</u>	<u>\$125,892,136</u>

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, 2013, the Municipality has \$7,006,932 of unexpended proceeds mainly from bond and notes issuances that are committed to future construction activities.

Additional information on the Municipality's capital assets can be found on Note 10 of the Basic Financial Statements.

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").

continue

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

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.

On June 30, 2013, the Municipality had \$93,269,558 in bonds, notes and other long-term debts outstanding, as compared to \$90,336,719 in prior year, a net increase of \$2,967,890, as shown in table below.

Under current state statutes, the Municipality required to limit the amount of general obligation debt to 10% of the total assessment of property located within the Municipality, for bonds to be repaid with the proceeds of property tax restricted for debt services.

LONG TERM LIABILITIES

<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>
General Obligation Bonds	\$37,750,000	\$ 505,000	\$ 3,236,000	\$35,019,000	\$3,467,000
Special Obligation Bonds	22,630,000	-	305,000	22,325,000	842,000
Property Tax Debt - Law 42	1,091,562	-	27,571	1,063,991	29,303
Property Tax Debt - Law 146	876,961	-	43,944	833,017	43,843
CRIM Final Liquidation 2012	1,347,602	-	-	1,347,602	1,347,602
CRIM Final Liquidation 2011	2,285,407	-	2,285,407	-	-
Department of Labor Debt	115,619	-	35,049	80,570	26,857
Christmas Bonus	803,093	717,916	803,093	717,916	717,916
Compensated Absences	5,684,382	-	622,073	5,062,309	876,075
Retirement System	-	2,780,184	-	2,780,184	1,286,976
Landfill Obligation	17,864,264	419,258	-	18,283,522	-
Claims and Judgments	690,922	5,065,525	-	5,756,447	-
Total	<u>\$91,139,812</u>	<u>\$ 9,487,883</u>	<u>\$ 7,358,137</u>	<u>\$93,269,558</u>	<u>\$ 8,637,572</u>

Additional information on the Municipality's long-term debt can be found on Note 11 of the Basic Financial Statements.

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. The General Fund next year 2013-2014 budget for resources and appropriations was approved in the amount of \$38,140,539. This amount represents a decrease of \$302,489 or 0.8% under fiscal year 2012-2013 actual amounts of resources on budgetary basis of \$38,543,028 and a decrease of \$2,996,392 or 7% under fiscal year 2012-2013 actual amounts of charges to appropriations on budgetary basis of \$41,136,931.

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

In Ordinances 28, 37 and 80 approved by the Municipal Legislature on January 15, January 29 and June 12, 2013, respectively, the legislative body authorized the Mayor to establish financial and administrative policies due to fiscal emergency. This Ordinances establish policies of personnel management, awarding of existent and future contracts, equipment acquisition, determining and collecting accounts receivable, legislative body expenditures, use of municipal vehicles, waste management, land disposition, use of facilities fees, sale of advertisement spots, service fees, reduction of legislators fee, and joint ventures with other government agencies and municipalities to provide services.

Federal and State grant revenues may vary if new grants are available but the revenues and expenditures are very predictable.

Those factors were considered when preparing the Municipality's budget for the fiscal year 2013-2014.

SUBSEQUENT EVENTS

Act No. 3 was enacted on April 4, 2013, amended the Act No. 447 for the purpose of establishing a major reform of the Commonwealth of Puerto Rico, Employees Retirement System (ERS) effective on July 1, 2013.

In August 2013 the Municipality of Arecibo entered into an agreement with the Commonwealth of Puerto Rico Retirement System, for the installment payment of its debt, stated as \$2,780,184 as of June 30, 2013 and increased to \$3,860,913 as of the date of the installment payment agreement. The agreement requires 36 monthly installments of \$107,247.53 until the liquidation of the debt.

In October 2013 the Municipality of Arecibo issued Municipal General Obligation Bonds in the amount of \$3,935,000 for the payment of operational debts. The bonds are payable on installments for a 25 years period.

In November 2013 the Municipality of Arecibo issued Municipal General Obligation Bonds in the amount of \$4,225,000 for the construction and improvements of capital projects. The bonds are payable on installments for a 20 years period.

As per Act Number 18 of 2014 was created the "Law of Municipal Administration Fund (MAF)" to establish a special fund called the Municipal Administration, authorize municipalities to pledge the funds deposited in the Local Government Fund to which they are to secure the repayment of any loan, bond note or other evidence of indebtedness, which are the source of repayment funds deposited in the Special Fund and to meet any expenditure budget of the Municipality and the Municipality any activity or project, authorize the Government Development Bank of Puerto Rico to make disbursements for purposes set out in this Act.

This measure is intended, first, to strengthen the financial capacity of the Corporation Tax Fund of Puerto Rico (COFINA, by Spanish acronyms), established under Law No. 91-2006, as amended, known as the "Law Fund of Sales and Usage Taxes", adjusting the sales and usage taxes (SUT) by increasing the state portion to 6.0% while the municipal SUT is reduced to 1.0% effective February 1, 2014.

continue

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO
MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Fiscal Year Ended June 30, 2013

Through this legislation a mechanism under which the SUT collections entitled to receive the Commonwealth of Puerto Rico each fiscal year after complying with the deposits in the Tax Fund requires by Act No. 91-2006, shall be deposited in a special fund created for the benefit of, and assigned to the municipalities. This special fund is called the "Local Government Fund" (LGF) which will be guarded by the Government Development Bank of Puerto Rico.

Also, on February 1, 2014 was enacted the Act No. 19 that creates the Municipal Financing Corporation (COFIM, by Spanish acronyms). The COFIM, attached to the Government Development Bank (GDB), with the power to issued bonds or use other mechanisms to pay or refinance debt incurred by municipalities, the payment of principal and interest is backed by the municipal SUT.

In addition, create the Redemption Fund of COFIM, to which the resources of the existing Municipal Fund Redemption will be transferred effective February 1, 2014, and facilitated the distribution of funds from the Municipal Redemption Fund, the Municipal Development Fund an the Municipal Improvement Fund. Provides that the first proceeds of the municipal SUT of 1% shall be collected by the Treasury Department and deposited directly into the Redemption Fund of COFIM. Provides that bonds and notes issued by the COFIM be payable and secured by the pledge of a fixed amount, or municipal SUT corresponding to a fixed rate of 0.3% has been collected during the previous fiscal year, whichever is greater.

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) 878-2299 or (787) 333-1063.

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	<u>GOVERNMENTAL ACTIVITIES</u>
ASSETS:	
Cash	\$ 6,554,916
Cash with Fiscal Agent	17,029,107
Receivables (Net):	
Federal Grants	771,689
Due from Government Units	1,464,787
Sales and Usage Taxes	<u>262,610</u>
Capital Assets:	
Land and Construction in Progress	62,812,853
Other Capital Assets [Net of Accumulated Depreciation]	<u>62,437,270</u>
Total Capital Assets	<u>125,250,123</u>
TOTAL ASSETS	<u>151,333,232</u>
LIABILITIES:	
Accounts Payable and Accrued Expenses	4,400,751
Accrued Interest	1,192,487
Due to Governmental Units	3,033,303
Unearned Revenues	6,022,697
Noncurrent Liabilities:	
Due Within One Year	8,637,572
Due in More than One Year	<u>84,631,986</u>
TOTAL LIABILITIES	<u>107,918,796</u>
NET POSITION:	
Net Investment in Capital Assets	85,120,257
Restricted for:	
Capital Projects	9,277,370
Debt Service	9,230,909
Other Purposes	1,450,502
Unrestricted (Deficit)	<u>(61,664,602)</u>
TOTAL NET POSITION	<u>\$ 43,414,436</u>

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues and Changes in Net Position
		Charges For Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Mayor and Municipal Legislature	\$ 2,661,062	\$ -	\$ -	\$ -	\$ (2,661,062)
General Government	29,377,792	-	379,363	-	(28,998,429)
Public Safety	4,260,765	-	-	-	(4,260,765)
Public Works	4,153,575	-	-	-	(4,153,575)
Culture and Recreation	2,696,093	300,362	-	-	(2,395,731)
Health and Sanitation	1,001,712	-	-	-	(1,001,712)
Solid Waste Disposal	1,088,811	455,716	-	-	(633,095)
Human Services and Welfare	6,578,516	-	6,685,913	-	107,397
Urban Development	2,478,557	-	2,418,247	-	(60,310)
Public Instruction	13,287,448	21,716	11,299,462	-	(1,966,270)
Landfill Closure and Post-Closure Care Costs	419,258	-	615,300	-	196,042
Interest on Long-Term Debt	2,820,844	-	-	-	(2,820,844)
Total Governmental Activities	\$ 70,824,433	\$ 777,794	\$ 21,398,285	\$ -	(48,648,354)
General Revenues:					
Taxes:					
					10,862,453
					5,306,478
					4,406,374
					6,286,528
					1,080,286
					15,245,792
					613,778
					<u>43,801,689</u>
					CHANGES IN NET POSITION
					(4,846,665)
					<u>48,261,101</u>
					NET POSITION – ENDING OF YEAR
					\$ 43,414,436

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

BALANCE SHEET – GOVERNMENTAL FUNDS
JUNE 30, 2013

	GENERAL FUND	HEAD START FUND	DEBT SERVICE FUND	CAPITAL ACTIVITIES FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS:						
Cash	\$ 4,424,262	\$ 412	\$ -	\$ 431,881	\$ 1,698,341	\$ 6,554,916
Cash with Fiscal Agent	153,968	-	9,854,519	7,006,932	13,688	17,029,107
Receivables:						
Property Taxes	263,400	-	568,877	-	-	832,277
Sales and Usage Taxes	262,610	-	-	-	-	262,610
Federal Grants	-	416,429	-	-	355,260	771,689
Due from Other Funds	475,322	393,180	-	9,140,938	150,000	10,159,440
Due from Governmental Units	632,510	-	-	-	-	632,510
Total Assets	\$ 6,212,092	\$ 810,021	\$ 10,423,396	\$ 16,579,751	\$ 2,217,289	\$ 36,242,549
LIABILITIES:						
Account Payable	\$ 3,580,762	\$ 186,311	\$ -	\$ 508,248	\$ 125,410	\$ 4,400,751
Bond Payable	-	-	3,706,000	-	-	3,706,000
Accrued Interest	-	-	1,192,487	-	-	1,192,487
Due to Governmental Units	3,033,303	-	-	-	-	3,033,303
Due to Other Funds	9,114,398	483,000	-	-	562,042	10,159,440
Unearned Revenues	5,702,652	140,710	-	-	179,335	6,022,697
Total Liabilities	21,431,135	810,021	4,898,487	508,248	866,787	28,514,678
DEFERRED INFLOWS OF RESOURCES:						
Unavailable Revenues - Commonwealth of Puerto Rico	622,358	-	568,877	-	-	1,191,235
Unavailable Revenues - Federal Grants	-	-	-	-	16,902	16,902
Total Deferred Inflows of Resources	622,358	-	568,877	-	16,902	1,208,137
FUND BALANCES (DEFICITS):						
Restricted	741,405	-	4,956,032	16,071,503	1,329,273	23,098,213
Committed	-	-	-	-	14,526	14,526
Assigned	-	-	-	-	-	-
Unassigned (Deficit)	(16,582,806)	-	-	-	(10,199)	(16,593,005)
Total Fund Balances	(15,841,401)	-	4,956,032	16,071,503	1,333,600	6,519,734
Total Liabilities, Deferred Inflows of Resources and Fund Balances (Deficits)	\$ 6,212,092	\$ 810,021	\$ 10,423,396	\$ 16,579,751	\$ 2,217,289	\$ 36,242,549

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

Total Fund Balances – Government Funds (Page 21)

\$ 6,519,734

Amount reported for Governmental Activities in the Statement of Net Position (Page 19)
 are different because:

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

Non Depreciable Capital Assets	\$ 62,812,853	
Depreciable Capital Assets	111,406,516	
Accumulated Depreciation	<u>(48,969,246)</u>	
Total Capital Assets		125,250,123

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

SBGP	16,902	
Christmas Bonus Reimbursement	358,958	
MRCC Liquidation	<u>832,277</u>	
Total Unavailable Revenues		1,208,137

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

General and Special Obligation Bonds	(53,638,000)	
Landfill Closure and Post-Closure	(18,283,522)	
Law 42	(1,063,991)	
Law 146	(833,017)	
MRCC Liquidation 2011-2012	(1,347,602)	
Department of Labor	(80,570)	
Retirement System	(2,780,184)	
Christmas Bonus	(717,916)	
Claims and Judgments	(5,756,447)	
Compensated Absences	<u>(5,062,309)</u>	
Total Noncurrent Liabilities		<u>(89,563,558)</u>

Total Net Position of Governmental Activities (Page 19)

\$ 43,414,436

COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE – GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	GENERAL FUND	HEAD START FUND	DEBT SERVICE FUND	CAPITAL ACTIVITIES FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
REVENUES:						
Property Taxes	\$ 10,599,053	\$ -	\$ 4,737,601	\$ -	\$ -	\$ 15,336,654
Volume of Business Taxes	6,286,528	-	-	-	-	6,286,528
Sales and Usage Taxes	3,413,925	-	992,449	-	-	4,406,374
Federal Grants	-	11,299,462	-	411,241	9,073,872	20,784,575
Intergovernmental	15,288,380	-	-	544,109	52,699	15,885,188
Construction Excise Taxes	1,080,286	-	-	-	-	1,080,286
Rent	300,362	-	-	-	-	300,362
Charges for Services	455,716	-	-	-	21,716	477,432
Miscellaneous	613,778	-	-	-	-	613,778
Total Revenues	38,038,028	11,299,462	5,730,050	955,350	9,148,287	65,171,177
EXPENDITURES:						
Current:						
Mayor and Municipal Legislature	2,660,676	-	-	-	-	2,660,676
General Government	23,831,549	-	-	148	148	23,831,845
Public Safety	4,009,196	-	-	-	-	4,009,196
Public Works	3,013,597	-	-	-	60,838	3,074,435
Culture and Recreation	1,742,882	-	-	-	-	1,742,882
Health and Sanitation	1,001,712	-	-	-	-	1,001,712
Solid Waste Disposal	1,088,811	-	-	-	-	1,088,811
Public Instruction	1,982,547	11,299,462	-	-	-	13,282,009
Human Services and Welfare	92,249	-	-	-	6,467,415	6,559,664
Urban Development	220,504	-	-	428,375	1,178,623	1,827,502
Capital Outlay	45,072	-	-	1,624,658	1,340,905	3,010,635
Debt Service:						
Principal	-	-	4,372,414	-	-	4,372,414
Interest and Other Charges	-	-	2,820,844	-	-	2,820,844
Total Expenditures	39,688,795	11,299,462	7,193,258	2,053,181	9,047,929	69,282,625
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(1,650,767)	-	(1,463,208)	(1,097,831)	100,358	(4,111,448)
OTHER FINANCING SOURCES (USES):						
Proceed of Bonds	505,000	-	-	-	-	505,000
Transfers – In	254,798	-	974,000	-	-	1,228,798
Transfers – Out	(974,000)	-	-	(169,062)	(85,736)	(1,228,798)
Total Other Financing Sources (Uses)	(214,202)	-	974,000	(169,062)	(85,736)	505,000
Net Change in Fund Balances	(1,864,969)	-	(489,208)	(1,266,893)	14,622	(3,606,448)
Fund Balances (Deficit), As Restated – Beginning	(13,976,432)	-	5,445,240	17,338,396	1,318,978	10,126,182
FUND BALANCES (DEFICIT) – ENDING	\$ (15,841,401)	\$ -	\$ 4,956,032	\$ 16,071,503	\$ 1,333,600	\$ 6,519,734

The accompanying Notes to the Basic Financial Statements are an integral part of this statement.

Net Change in Fund Balances – Government Funds (Page 23) \$ (3,606,448)

Amount reported for Governmental Activities in the Statement of Activities (Page 20)
 are different because:

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

Capital Outlays	\$ 3,010,635	
Depreciation Expense	<u>(3,652,648)</u>	
Excess of Depreciation Expense over Capital Outlays		(642,013)

Revenues in the Statement of Activities that do not provide current financial resources are
 reported as revenues in the funds and vice versa:

SBGP	16,902	
Christmas Bonus	(42,588)	
MRCC Liquidation	<u>832,277</u>	
Total of Revenues		806,591

Bonds proceeds provide current financial resources to governmental funds, but issuing debt
 increase Noncurrent Liabilities in the Statement of Net Position. In the current period,
 proceeds received was (505,000)

Repayment of long-term principal is expenditure in the governmental funds, but issuing debt
 reduced Noncurrent Liabilities in the Statement of Net Position. In the current period
 repayments were 4,372,414

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

Decrease in Christmas Bonus	85,177	
Increase in Retirement System Debt	(2,780,184)	
Decrease in MRCC Liquidation	2,285,407	
Increase in Landfill Closure and Post-Closure Care Costs	(419,258)	
Increase in Claims and Judgments	(5,065,424)	
Decrease in Compensated Absence	<u>622,073</u>	
Total Additional Expenses		<u>(5,272,209)</u>

Change in Net Position of Governmental Activities (Page 20) \$ (4,846,665)

1. FINANCIAL REPORTING ENTITY

The accompanying financial statements present information on the financial activities of the Autonomous Municipality of Arecibo of the Commonwealth of Puerto Rico (Municipality) over which the Mayor and the Municipal Legislature, have direct or indirect governing and fiscal control. These financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP).

A. Organization

The Municipality was founded in the year 1515, and operates as a governmental unit of the Commonwealth of Puerto Rico (Commonwealth), under the Act Number 81 of August 30, 1991, known as "Autonomy Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the Municipality is composed of the executive and legislative bodies. The Municipality is governed by a Mayor and is elected every four years in the general elections of the Commonwealth. The legislative body (Municipal Legislature) consists of 16 Legislators also elected in the general elections of Puerto Rico for a four-year period.

The Municipality provides services such as: health, public works, sanitation, aids and services to low-income and elderly citizens, public safety, housing and urban development, culture and recreation, planning, zoning and other general and administrative services. As a government entity, the Municipality is exempt from both federal and state taxes.

B. Reporting Entity

A reporting entity is comprised of (1) the primary government, (2) component unit organizations for which the primary government is financial accountable (blended component units), and (3) other organizations for which the nature and significance of their relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete, and they are financially accountable to the primary government (discrete component units). The primary government consists of all funds, departments, boards and agencies that are not legally separate from the Municipality and for which the Municipality is financial accountable.

The accompanying basic financial statements include all departments and organizations units whose funds are under the custody and control of the Municipality. In evaluating the Municipality as a reporting entity, management has addressed all the potential component units. GASB Accounting Standards Codification Section 2600, *Reporting Entity and Component Unit Presentation and Disclosure*, requires the inclusion of organizations that raise and hold funds for the direct benefit of the primary government.

GASB Accounting Standards Codification Section 2100, *Defining the Financial Reporting Entity*, describes the criteria for determining which organizations, functions, and activities should be considered part of the Municipality for financial reporting purposes. The primary criteria include appointing a voting majority of an organization's governing body, and the Municipality's ability to impose its will on that organization or the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Municipality.

A legally separate, tax-exempt organization should be discretely presented as a component unit if all of the following criteria are met: (a) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (b) the primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (c) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

The Governmental Accounting Standards Board (GASB) has issued Statement 61, *The Financial Reporting Entity: Omnibus an Amendment of GASB Statements No. 14 and No. 34*. GASB 61 provides additional criteria for classifying entities as component units to better assess the accountability of elected officials by ensuring that the financial reporting entity includes only organizations for which the elected officials are financially accountable or that are determined by the government to be misleading to exclude. The Municipality adopted this statement effective July 1, 2012.

There are two methods of presentation of the component unit in the financial statements: 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; and discrete – presentation of the component unit's financial data in column separate from the Municipality's balances and transactions. The relative importance of each criterion must be evaluated in light of specific circumstances in order to determine which components units are to be included as part of the reporting entity. Based on these criteria, there are no other organizations which should be included in these basic financial statements.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These financial statements present the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2013, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

A. Financial Statement Presentation

The basic financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America as applicable to local governmental units. The basic financial statements include both government-wide (based on the Municipality as a whole) and fund financial statements, which provide a more detailed level of financial information. Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as governmental type.

The financial information of the Municipality is presented in this report as follows:

Required Supplementary Information – Management’s Discussion and Analysis

Management’s Discussion and Analysis is required supplementary information that introduces the basic financial statements and provides an analytical overview of the Municipality’s financial activities.

Government-wide Financial Statements (GWFS)

While separate government-wide and fund financial statements are presented, they are interrelated. The GWFS (the *Statement of Net Position* and the *Statement of Activities*) report information of all the activities of the Municipality. For the most part, the effect of interfund activity has been removed from these financial statements. Exceptions to this general rule are payments in lieu of taxes where the amounts are reasonably equivalent in value to the interfund services provided and other charges between the government’s Puerto Rico Electric Power Authority function of the government. Elimination of this charges would distort the direct cost and program revenue reported for the various functions concerned. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely, to a significant extent, on fees and charges to external customers for support.

The focus of the *Statement of Net Position* is designed to be similar to bottom line results for the Municipality’s governmental activities and business type activities. This statement combines and consolidates governmental fund’s current financial resources (short-term spendable resources) with capital assets and long-term obligations. The *Statement of Net Position* presents the reporting entities’ assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net positions. Net positions are classified as net investment in capital assets, restricted when constraints are placed on them that are imposed by external parties or by laws or regulations, and unrestricted. Designations solely imposed by the Municipality’s management are not presented as restricted net position. When both restricted and unrestricted resources are available for use, the Municipality’s policy is to use the restricted resources first.

The *Statement of Activities* demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. In addition, to the extent that indirect costs are allocated to the various functions, the program expenses will include both direct and indirect costs. *Program Revenues* include charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment, and grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Taxes and other items properly excluded from program revenues are reported instead as *general revenues*.

Governmental Funds Financial Statements (GFFS)

The GFFS [the *Balance Sheet*, and the *Statement of Revenues, Expenditures and Changes in Fund Balance*] provide information about the Municipality’s funds. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. Non-major funds are summarized into a single column.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

This presentation deemed most appropriate to (1) demonstrate legal and covenant compliance, (2) demonstrate the source and use of liquid resources, and (3) demonstrate how the Municipality's actual experience conforms to the budgeted fiscal plan.

The Municipality reports the following major governmental funds:

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

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

Capital Activities Fund – This fund is used to account for and report financial resources that are restricted or committed to expenditure for capital outlays, including the acquisition or construction of major capital facilities, including those outlays financed by the general obligation bond proceeds.

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

The non-major funds are combined in a single column in the GGFS. As a general rule the effect of interfund activity has been eliminated from the GWFS.

Since the GFFS are presented in different measurement focus and basis of accounting than the GWFS, reconciliation is presented and separate explanation for each differences.

The Municipality periodically undertakes a comprehensive evaluation of its fund structure to ensure that it complies with all aspects that are of importance to users of general purpose external financial reports. Consequently, all superfluous funds and some operational funds currently used by the Municipality in the day-to-day accounting procedures have not been reported as individual governmental funds in the accompanying fund financial statements. Accordingly, the accompanying fund financial statements include only the minimum number of funds consistent with legal and operating requirements and, consequently, certain types of similar operational funds have been combined into single funds in the accompanying fund financial statements.

The financial statements of the governmental funds are the following:

Balance Sheet – Reports information at June 30, 2013 about the current financial resources (assets, liabilities, deferred inflows of resources and fund balances) of each major governmental fund.

Statement of Revenues, Expenditures and Changes in Fund Balance – Reports information about the inflows, outflows and balances of current financial resources of each major governmental fund for the fiscal year ended June 30, 2013.

Notes to the Basic Financial Statements

The notes to the financial statements provide information that is essential to a user's full understanding of the data provided in the basis financial statements.

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information. This section includes a *Budgetary Comparison Schedule – General Fund*, which includes reconciliation between the statutory fund balance for budgetary purposes and the fund balance for the General Fund as presented in the GFFS.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

B. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

Government-wide Financial Statements

The government-wide financial statements are reported using the *economic resources measurement focus* and the *full accrual basis of accounting*. Revenue (including interest on deposits and investments) is generally recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Nonexchange transactions, in which the Municipality gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Nonexchange transactions, in which the Municipality gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Receipts on any type of revenue sources collected in advance for use in the following fiscal year are recorded as unearned revenues.

Governmental Funds Financial Statements

The GFFS are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Under this method, 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 these purposes, the Municipality considers revenues to be available if they are collected within sixty (60) days after the end of the current fiscal period. Revenues that the Municipality earns by incurring obligations are recognized in the same period as when the obligations are recognized. At June 30, 2013, all revenues sources met this availability criterion.

Property taxes, volume of business taxes, sales and usage taxes, construction excise taxes, 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. Entitlements are recorded as revenues when all eligibility requirements are met, including any time requirements and the amount is received during the period or within the availability requirements have been met, and the amount is received during the period or within the availability period for this revenue source (60 days of year-end). Expenditures-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the Municipality.

Expenditures are recorded when the related fund liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, and claims and judgments, are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Principal and interest on bonds payable are recorded when they matured (when payment is due), except for principal and interest of bonds due on July 1, 2013, which are recorded as governmental fund liabilities of June 30, 2013 which is the date when resources were available in the debt service fund. Proceeds of general long-term debt and acquisitions under capital leases, if any, are reported as other financing sources.

The accompanying Balance Sheet – Governmental Funds generally reflects only assets that will not be converted into cash to satisfy current liabilities. Long-term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying Balance Sheet – Governmental Funds.

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

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

C. Stewardship, Compliance, and Accountability

Budgetary Information

The Municipality's annually adopts the Budget Resolution for all operating funds of the Municipality except for certain restricted accounts. Budgetary control is legally maintained at the fund level. The budget is prepared using the modified accrual basis of accounting with encumbrance included as budgetary basis expenditures. Unexpended appropriations at the end of the fiscal year generally lapse. However, they may be re-appropriated for expenditures in the following fiscal year.

The Municipality's Budget Resolution provides transfer authority (1) to the Mayor and the Management and Budget Director, within and between departments and funds, as long as the total budget of the Municipality (net of interfund transfers) is not increased; (2) to the Management and Budget Director to implement grant budgets as the grant applications are accepted by the Municipality; and (3) to the Management and Budget Director to amend (re-appropriate) each new year's budget, to the extent of outstanding encumbrances, and/or unexpended project/grant appropriations at year end. Municipality's Legislature action is required for (1) use of the budgeted Legislature contingency, and (2) the approval of a supplemental appropriation(s). During the year, several supplemental appropriations were necessary.

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

The unencumbered balance of any appropriation at the end of the 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 Municipality follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the Budgetary Comparison Schedule – General Fund:

Original Budget

1. Prior of May 15 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message.
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature.
3. The Office of the Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law.
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance to be effective on July 1.

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

Final Budget

The final budgetary data presented in the Budgetary Comparison Schedule – General Fund reflects the following changes to the original budget:

1. Certain annual appropriations are budgeted on a project basis. If such projects are not completed at the end of the fiscal year, unexpended appropriations, including encumbered funds, and unexpended grant appropriations, are carried forward to the following year. In certain circumstances, other regular annual appropriations may be carried forward after appropriate approval. Annually appropriated funds, not authorized to be carried forward, lapse at the end of the fiscal year. Appropriations carried forward from the prior year are included in the final budgetary data.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

2. Appropriations may be adjusted during the year with the approval of the Mayor and the Municipal Legislature, e.g. supplemental appropriations. Additionally, the Mayor is authorized to make certain transfer of surplus within the departments. Such adjustments are reflected in the final budgetary data.

The Annual Appropriation Ordinance adopts the budget at the character level of expenditure within departments. As described above, the Mayor is authorized to make certain transfers of appropriations within departments. Accordingly, the legal level of budgetary control by the Municipal Legislature is the department Level.

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

1. Encumbrances are recorded as expenditures under the budgetary basis and as restricted, committed and assigned fund balances under GAAP.
2. Interfund transactions of the General Fund are not included in the budgetary basis.
3. Certain accrued liabilities and other debts are not included in the budgetary basis.
4. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

Excess of Expenditures over Appropriations

For the year ended June 30, 2013, expenditures exceeded appropriations in the general government function of the general fund by \$3,750,306. While overspending of this appropriation is authorized by law up to \$100,000 if related to cases involving imminent public endangerment (e.g., the need to inspect properties with damage from collision, natural disaster, fire, or water to determine their inherent stability), which was the case this year, it is nevertheless considered a budgetary violation. Further, the overspending comes with a consequence for the subsequent year's budget.

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

D. Assets, Liabilities, and Net Position

1) *Cash, Cash Equivalent, and Cash with Fiscal Agent*

The Municipality's cash and investment are composed of demand deposits in commercial banks, demand deposits in the Governmental Development Bank of Puerto Rico (GDB), and cash equivalents in commercial banks. The Municipality has adopted the *Statement of Uniform Investment Guidelines for the Municipalities of the Commonwealth of Puerto Rico*, issued by the GDB as promulgated by Act No. 113 of August 3, 1995. The Finance Director of the Municipality, follow the guidelines, is responsible for investing the available resources in certificates of deposit and other short-term investments. Investments are made from the available combined funds of the Municipality and, accordingly, it is not practical to disclose certificates of deposit and other short-term investments individually by fund in the combined financial statements. Interest earned on certificates of deposit and interest bearing commercial bank accounts are recognized as revenue in the General Fund. Cash in the Special Revenue and Capital Project Funds are restricted; accordingly, resources available were not used for pool investments. Cash Equivalents are investments with an original maturity of 90 days or less.

Cash with fiscal agent in the Debt Service Fund represents special additional property tax collections retained by the Commonwealth, deposit in the GDB and restricted for the payment of the Municipality's debt service, as established by law. Cash with fiscal agent in other governmental funds consists of undisbursed proceeds of certain bonds and notes issued for the acquisition and construction of major capital improvements, or grants which are maintained in a cash custodian account by the GDB. This sinking fund is maintained by the GDB, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

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." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statement as "interfund balances".

Advance 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 consist of all revenues earned but not collected at June 30, 2013. These account receivables are shown net of estimated allowances for uncollectible accounts, which are determined upon past collection experience, historical trends, and current economic conditions. Intergovernmental receivables in the general fund represent mostly sales and usage taxes, federal grant and contributions, property tax accounts that are levied by Municipal Revenue Collection Center (MRCC), a governmental entity created by the Commonwealth. Intergovernmental receivables in the other governmental funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded grant and contributions and state appropriations, and the amount in the debt service fund represents the distribution of property tax collected which is restricted for the debt service.

Accounts payable represent amounts, including salaries and wages, owed for goods and services received prior to year-end.

3) *Inventories*

The Municipality used the purchase method to account for the purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. This method records items as expenditures, in the appropriate fund, when they are acquired and, accordingly, the inventory is not recorded in the basic financial statements.

4) *Capital Assets*

Capital assets, which include land, buildings and improvement, machinery and equipment, motor vehicles, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the GWFS. Capital assets, other than infrastructure assets, are defined by the Municipality as assets with an initial, individual cost of more than \$25 (amount not rounded) and an estimated useful life in excess of two years. For improvements other than buildings, the capital outlay must be greater than \$10,000, extend the estimated useful life for ten years, and be greater than 10% of the original cost of the asset. The Municipality reports infrastructure assets on a network and subsystem basis. Accordingly, the amounts spent for the construction or acquisition of infrastructure assets are capitalized and reported in the government-wide financial statements regardless of their amount.

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by governmental activities) the Municipality chose to include all such items regardless of their acquisition date or amount.

The Municipality was able to estimate the historical cost for the initial reporting of these assets through back trending (i.e., estimating the current replacement cost of the infrastructure to be capitalized and using an appropriate price-level index to deflate the cost to the acquisition year or estimated acquisition year). As the Municipality constructs or acquires additional capital assets each period, including infrastructure assets, they are capitalized and reported at historical cost. The reported value excludes normal maintenance and repairs which are essentially amounts spent in relation to capital assets that do not increase the capacity or efficiency of the item or extend its useful life beyond the original estimate. In the case of donations the Municipality values these capital assets at the estimated fair value of the item at the date of its donation.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

Capital outlay is recorded as expenditures of the General Fund and other governmental funds and as assets in the GFFS to the extent the Municipality capitalization threshold is met. Depreciation and amortization expense is recorded only in the GWFS. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight-line method, except for equipment held under capital leases which is depreciated over the shorter of its estimated useful life or the lease term. No depreciation is recorded for land and construction in progress. The estimated useful lives of major capital asset categories are:

DESCRIPTION	YEARS
Buildings and Improvement	40
Infrastructure	40
Vehicles	5
Furniture and Fixtures	5
Machinery and Equipment	3-5

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

The accounting policy for Works of Art is that they are capitalized at their historical cost or fair value at date of donation whether they are held as individual items or in a collection. Capitalized collections or individual items that is exhaustible, such as exhibits whose useful lives are diminished by display or educational or research applications, are depreciated over their estimated useful lives. Depreciation is not required for collections or individual items that are inexhaustible. At June 30, 2013, all Work of Art are considered inexhaustible.

Impaired capital assets that will no longer be used by the Municipality, if any, are reported at the lower of carrying value or fair value. Impairment losses on capital assets with physical damages that will continue to be used by the Municipality are measured using the restoration cost approach. Impairments of capital assets that are subject to a change in the manner or duration of use, or assets affected by enactment or approval of laws or regulations or other changes in environmental factors or assets that are subject to technological changes or obsolescence, if any, are measured using the service units approach.

5) Deferred Outflows/Inflows of Resources

In addition to assets, the *Statement of Net Position* will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense/expenditure) until then. The Municipality has no items that qualify for reporting in this category.

In addition to liabilities, the *Statement of Net Position* will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Municipality has no items that qualify for reporting in this category.

The Municipality has items, which arises only under a modified accrual basis of accounting that qualifies for reporting in deferred inflows of resources. Accordingly, the items, *unavailable revenue*, is reported only in the governmental funds Balance Sheet. The governmental funds report *unavailable revenues* from three sources: Christmas Bonus Reimbursement from the Commonwealth, Property Taxes from MRCC liquidation, and Federal Grants. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available.

6) Unearned Revenues

In the GWFS, deferred revenues arise only when the Municipality receives resources before it has a legal claim to them. In the GFFS, arises when the following situations occur: potential revenue does not meet both the measurable and available criteria for revenue recognition in the current period.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

7) *Long-Term Obligations, Bonds Issuance Costs, and Premium or Discount*

The liabilities reported in the GWFS include the general and special obligation bonds, long-term notes, other noncurrent liabilities (e.g., vacation, sick leave, claims and judgments, noncurrent liabilities to other governmental entities and third parties, and landfill post closure care costs). Bond premiums and discounts, if any, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount, if any. As per GASB Statement No. 65, Bond Issuance Costs incurred are reported as expense in the fiscal year incurred.

In the GFFS, governmental fund types recognize bond premiums and discounts as other financing sources and uses, respectively, and bond issuance costs as debt service expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures. Expenditures for principal and interest payments for governmental fund general and special obligations bonds are recognized in the Debt Service Fund when due.

8) *Compensated Absences*

The Municipality accrues accumulated unpaid vacation and sick leave and associated employee-related costs when earned (or estimated to be earned) by the employee. The Municipality's employees are granted 30 days of vacations and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of sixty (60) days and sick leave up to a maximum of ninety (90) days. In the event of employee resignation, the employee is paid for accumulated vacation days up to the maximum allowed at the current rate. Separation from employment prior to use of all or part of the sick leave terminates all rights for compensation, except for employees with ten years of service who are entitled to sick leave pay up to the maximum allowed. The Municipality accrued a liability for compensated absences, which meet the following criteria: (1) the Municipality's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered; (2) the obligation relates to rights that vest or accumulate; (3) payment of the compensation is probable; and (4) the amount can be reasonably estimated.

In accordance with the above criteria and requirements in conformance with GASB Accounting Standards Codification Section C60, *Compensated Absences*, the Municipality has accrued a liability for compensated absences, which has been earned but not taken by Municipality's employees, including its share of social security and Medicare payments made on behalf of the employees in the accrual for vacation and sick leave pay using salary rates effective at June 30, 2013. All vacation pay is accrued when incurred in the GWFS. For the GWFS, the current portion is the amount estimated to be used in the following year. For the GFFS, all of the compensated absences are considered long-term and therefore, are not a fund liability and represents a reconciling item between the fund level and government-wide presentations.

9) *Claims and Judgments*

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

10) *Accounting for Pension Costs*

The Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

For the purpose of applying the requirements of GASBS No. 27, as amended, the state government of the Commonwealth is considered to be the sponsor of the Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (ERS), a multiemployer cost-sharing defined benefit pension plan and System 2000, a hybrid defined contribution plan, in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Commonwealth and the basic financial statements of such retirement systems are part of the financial reporting entity of Commonwealth. Act No. 3 was enacted on April 4, 2013, amended the Act No. 447 for the purpose of establishing a major reform of the ERS effective on July 1, 2013 (see Note 18).

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

11) Landfill

As per requirements of State and Federal laws and regulations the Municipality should be obligated to place a final cover on its closed landfill and perform certain maintenance and monitoring functions at the landfill site for the next thirty years (See Note 11). The estimated liability for municipal solid waste landfill post-closure care costs (including monitoring and maintenance) include an estimate of all post-closure care costs to be incurred in the Municipality's closed solid waste landfill, and is recorded as a liability in the accompanying GWFS, *Statement of Net Position*, under the provisions of GASB Accounting Standards Codification Section L 10, *Landfill Closure and Post-Closure Care Costs*.

The estimates post-closing costs are made using current costs. The liability should be adjusted annually to reflect the effects of inflation, advances in technology, changes in regulations or similar changes.

At the governmental funds' level, landfill post-closure care costs do not constitute an outflow of current financial resources and should not result in the recognition of a governmental fund liability or expenditures. Post-closure care costs are recorded in the *Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds* as expenditures in the accounting period in which the payments are made.

12) Net Position/Fund Balance

A) Net Position

Net position represent the difference between assets, deferred outflows of resources, liabilities, and deferred inflows of resources in the government-wide financial statements.

The GWFS utilize a net position presentation, which are categorized as follow:

- *Net Invested in Capital Assets* – These consists of capital assets, net of accumulated depreciation and amortization, reduced by the outstanding balances of bonds payable, notes payable and other debts that are attributed to the acquisition, construction or improvements of those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvements of capital assets has been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs. In addition, the outstanding debt attributed to capital assets does not include accrued interest payable, non-capital accrued liabilities, inter-fund loans and other financial assets.

Net investment in capital assets is comprised of the following:

	<u>Governmental Activities</u>
Capital Assets, Net of Accumulated Depreciation	\$125,250,124
Outstanding Balance on Related Debt.....	(46,924,000)
Unspent Capital Debt Proceeds.....	<u>6,794,133</u>
Net Investment in Capital Assets	<u>\$ 85,120,257</u>

- *Restricted Net Position* – These result when constraints placed on net position use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted Net Position* – These consist of net position which do not meet the definition of the two preceding categories. Unrestricted net position often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net position often have constraints on resources that are imposed by management, but can be removed or modified.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

Net Position Flow Assumption

Sometimes the Municipality will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the government-wide and proprietary fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the Municipality's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

B) *Fund Balance*

Fund Balance Classification

Fund balances for the governmental funds are reported in classifications that comprise a hierarchy based on the extent to which the Municipality honors constraints on the specific purposes for which amounts in those funds can be spent.

The nonspendable classification contains amounts not in spendable form or legally or contractually required to be maintained intact. Restricted amounts contain restraints on their use externally imposed by creditors, grantors, contributors, or laws or regulation of other governments; or imposed by law through constitutional provisions or enabling legislation. Committed amounts can only be used for specific purposes imposed by formal action of the Municipality's highest level of decision-making authority. The highest level of decision-making authority is the Municipal Legislature and it takes a resolution to establish a fund balance commitment. Amounts intended to be used for specific purposes are assigned. Assignments should not cause deficits in the Unassigned Fund Balance. Unassigned Fund Balance is the residual classification for the General Fund.

Fund Balance Flow Assumption

Sometimes the Municipality will fund outlays for a particular purpose from both restricted and unrestricted resources (the total committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the GFFS a flow assumption must be made about the order in which the resources are considered to be applied. It is the Municipality's policy to consider restricted fund balance to have been depleted before using any of the components or unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

Fund Balance Policy

The Municipality believes that sound financial management principles require that sufficient funds be retained by the Municipality to provide a stable financial base at all times. To retain this stable financial base, the Municipality needs to maintain a General Fund balance sufficient to fund all cash flows of the Municipality, to provide financial reserves for unanticipated expenditures and/or revenue shortfalls of an emergency nature, to provide funds for the disparity in timing between the collection of property taxes and other main income. The purpose of this policy is to specify the size and composition of the Municipality's financial reserves and to identify certain requirements for replenishing any fund balance reserves utilized.

Policy on Committing Funds

It is the policy of the Municipality that fund balance amounts will be reported as "Committed Fund Balance" only after formal action and approval by Municipal Legislature. The Municipal Legislature has the authority to separate funds for specific purposes. Any separate fund as Committed Fund Balance requires the adoption of a resolution by a simple majority of votes. The adoption of the resolution should be carried out before June 30 of the fiscal year to implement. If the actual amount of the commitment is not available through June 30, the resolution should establish the process or formula required to calculate the exact amount as soon as information is available in the following fiscal year.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

For example, the Municipal Legislature may approve a resolution prior to year-end financial statements, if available, up to a specified dollar amount as Committed Fund Balance for capital projects. The exact dollar amount to be reported as Committed Fund Balance for capital projects may not be known at the time of approval due to the annual financial audit not yet being completed. This amount can be determined at a later date when known and appropriately reported within the year-end financial statements due to the Municipal Legislature approving this resolution before year-end.

It is the policy of the Municipality that the Municipal Legislature may commit fund balance for any reason that is consistent with the definition of Committed Fund Balance. Examples of reasons to commit fund balance would be to display intentions to use portions of fund balance for future capital projects, stabilization funds, or to earmark special General Fund streams unspent at year-end that are intended to be used for specific purposes.

After approval by the Municipal Legislature, the amount reported as Committed Fund Balance cannot be reversed without utilizing the same process required to commit the funds. Therefore, it is the policy of the Municipality that funds can only be removed from the Committed Fund Balance category after resolution and approval by the Municipal Legislature.

Policy on Assigning Funds

Funds that are *intended* to be used for a specific purpose but have not received the formal approval action at the Municipal Legislature level may be recorded as Assigned Fund Balance. Likewise, redeploying assigned resources to an alternative use does not require formal action by the Municipal Legislature. Having reviewed the requirements for assigning fund balance, therefore, is the policy of the Municipality that Mayor shall have the authority to assign fund balance of the Municipality based on the intentions of the use of funds by the Municipal Legislature. In addition, the Mayor can delegate to the Finance Director or other employee of the Municipality, the authority to assign the funds.

Policy on Unassigned General Fund Balance

It is the goal of the Municipality to achieve and maintain an Unassigned General Fund Balance equal to 10% of budgeted expenditures. The Municipality considers a balance of less than 5% to be a cause for concern, barring unusual or deliberate circumstances, and a balance of more than 15% as excessive. An amount in excess of 15% is to be considered for reservation to accumulate funding for purchase of machinery and equipment, for capital projects, and/or to reduce the tax levy requirements, and shall be determined in conjunction with the annual budget process. In the event that the Unassigned General Fund Balance is less than the policy anticipates, the Municipality shall plan to adjust budget resources in the subsequent fiscal years to restore the balance. Appropriation from Unassigned General Fund Balance shall require the approval of the Municipal Legislature and shall be only for specific disbursements, such as one-time expenditures and capital assets purchases, and not for ongoing expenditures unless a viable plan designated to sustain the expenditures is simultaneously adopted. The Municipality has met its GASB 54 fund balance targets at June 30, 2013.

Prioritization of Fund Balance Use

In circumstances where expenditure is for a purpose that quantities are available in multiple fund balance classifications, the order in which the resources will be used shall be as follows: Restricted Fund Balance, followed by Committed Fund Balance, Assigned Fund Balance, and last but not least, Unassigned Fund Balance.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

C) Components of Fund Balance

	GENERAL FUND	HEAD START FUND	DEBT SERVICE FUND	CAPITAL ACTIVITIES FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
Nonexpendable	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Restricted For:						
Improvement of Streets and Sidewalks	-	-	-	3,732,984	-	3,732,984
Improvement and Construction of Facilities	-	-	-	3,248,869	15,100	3,263,969
Capital Outlay	-	-	-	164,957	-	164,957
Improvement of Water and Sewer System	-	-	-	4,335,141	-	4,335,141
Welfare	-	-	-	-	1,071,391	1,071,391
Debt Repayment	-	-	4,956,032	-	-	4,956,032
General Government	741,405	-	-	4,589,552	242,782	5,573,739
Total Restricted	741,405	-	4,956,032	16,071,503	1,329,273	23,098,213
Committed To:						
Welfare	-	-	-	-	14,526	14,526
Total Committed	-	-	-	-	14,526	14,526
Assigned	-	-	-	-	-	-
Unassigned (Deficit)	(16,582,806)	-	-	-	(10,199)	(16,593,005)
Total Fund Balances	\$ (15,841,401)	\$ -	\$ 4,956,032	\$ 16,071,503	\$ 1,333,600	\$ 6,519,734

E. Interfund Transactions

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

Interfund Transfers – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds.

Intra-Entity Transactions – Advances between funds are also presented as amounts due to and due from other funds. However, these transfers and related amounts receivables and payables are considered internal balances and activities that have been eliminated in the government-wide financial statements.

F. Risk Financing

The Municipality carries commercial insurance to cover property and 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. Also, principal officials of the Municipality are covered under various surety bonds. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the MRCC for the year ended June 30, 2013 amounted to approximately \$1,114,842. The current insurance policies have not been cancelled or terminated.

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

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

The Municipality obtains workers compensation insurance through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth of Puerto Rico. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the MRCC for the year ended June 30, 2013 amounted to \$758,297.

The Municipality obtains unemployment compensation, non-occupational disability, and drivers' insurance coverage for its employees through various insurance programs administered by the Department of Labor and Human Resources of the Commonwealth of Puerto Rico (DOLHR). These insurance programs cover workers against unemployment and provide supplementary insurance coverage for temporary disability, or death because work or employment-related accidents or non-occupational disability and drivers' insurance premiums are paid to DOLHR on a cost reimbursement basis.

Under Act No. 63 of June 21, 2010, the Legislative Assembly of the Commonwealth of Puerto Rico, authorized the municipalities to procure and manage at their own discretion all insurance policies, including those related to health plans been provided to the municipal employees. The Municipality also obtains medical insurance coverage from one health insurance company for its employees. Different health coverage and premium options are negotiated each year by the Municipality. Premiums are paid on a monthly basis directly to the insurance company.

G. Use of Estimates

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

H. Reclassifications

Various reclassifications have been made in the accompanying basic financial statements which affect the comparability with the basic financial statements issued for previous fiscal years.

I. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) issued the following pronouncements that have effective dates after June 30, 2013:

GASB Statement No. 66, Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, and No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.

This Statement amends Statement No. 10, Accounting and Financial Reporting for Risk Financing and Related Insurance Issues, by removing the provision that limits fund-based reporting of an entity's risk financing activities to the general fund and the internal service fund type. As a result, governments should base their decisions about fund type classification on the nature of the activity to be reported, as required in Statement 54 and Statement No. 34, Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments.

This Statement also amends Statement 62 by modifying the specific guidance on accounting for (1) operating lease payments that vary from a straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. These changes clarify how to apply Statement No. 13, Accounting for Operating Leases with Scheduled Rent Increases, and result in guidance that is consistent with the requirements in Statement No. 48, Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues, respectively. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012 (FY 2013-2014). Earlier application is encouraged.

continue

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – continuation

GASB Statement No. 67, *Financial Reporting for Pension Plans*. This Statement replaces the requirements of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* and Statement No. 50, *Pension Disclosures—an amendment of GASB Statements No. 25 and No. 27*, as they relate to pension plans that are administered through trusts or similar arrangements meeting certain criteria. The Statement builds upon the existing framework for financial reports of defined benefit pension plans, which includes a statement of fiduciary net position (the amount held in a trust for paying retirement benefits) and a statement of changes in fiduciary net position. Statement No. 67 enhances note disclosures and RSI for both defined benefit and defined contribution pension plans. Statement No. 67 also requires the presentation of new information about annual money-weighted rates of return in the notes to the financial statements and in 10-year RSI schedules. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2013 (FY 2013-2014). Earlier application is encouraged.

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This Statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and Statement No. 50, *Pension Disclosures—an amendment of GASB Statements No. 25 and No. 27* as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement No. 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. The Statement also enhances accountability and transparency through revised and new note disclosures and required supplementary information. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2014 (FY 2014-2015). Earlier application is encouraged.

GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*. This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term *government combinations* includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2013 (FY 2014-2015). Earlier application is encouraged.

GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. This Statement requires a government that has issued an obligation guaranteed in a nonexchange transaction to recognize revenue to the extent of the reduction in its guaranteed liabilities. This Statement also requires a government that is required to repay a guarantor for making a payment on a guaranteed obligation or legally assuming the guaranteed obligation to continue to recognize a liability until legally released as an obligor. When a government is released as an obligor, the government should recognize revenue as a result of being relieved of the obligation. This Statement also provides additional guidance for intra-entity nonexchange financial guarantees involving blended component units. This Statement specifies the information required to be disclosed by governments that extend nonexchange financial guarantees. In addition, this Statement requires new information to be disclosed by governments that receive nonexchange financial guarantees. The provisions of this Statement are effective for reporting periods beginning after June 15, 2013 (FY 2013-2014). Earlier application is encouraged.

GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date—an amendment of GASB Statement No. 68*. This Statement eliminates a potential source of understatement of restated beginning net position and expense in a government's first year of implementing GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. To correct this potential understatement, Statement 71 requires a state or local government, when transitioning to the new pension standards, to recognize a beginning deferred outflow of resources for its pension contributions made during the time between the measurement date of the beginning net pension liability and the beginning of the initial fiscal year of implementation. This amount will be recognized regardless of whether it is practical to determine the beginning amounts of all other deferred outflows of resources and deferred inflows of resources related to pensions. The provisions are effective simultaneously with the provisions of Statement 68, which is required to be applied in fiscal years beginning after June 15, 2014 (FY 2013-2014).

The Municipality has not yet determined the effect these statements will have on the Municipality's financial statements.

continue

3. CASH AND INVESTMENTS

Cash in Banks

Municipality's cash and investments at June 30, 2013 are composed of: (1) demand deposits in commercial banks, (2) demand deposits in the Government Development Bank of Puerto Rico (GDB, fiscal agent), and (3) cash equivalents in commercial banks. Cash equivalents of \$23.6 million are deposits in commercial bank accounts and interest bearing accounts in GDB, and are recorded at cost, which approximates fair value.

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

Municipality follows the practice of pooling cash. At June 30, 2013, the pool cash account in interest bearing commercial banks accounts had a balance of \$6.6 million of which \$4.4 million in the General Fund, \$412 in the Head Start Fund, \$431,881 in the Capital Activities Fund, and \$1.7 million in Other Governmental Funds. The balance in the pooled cash account is available to meet current operating requirements and any unrestricted excess, if any, is generally deposit in accounts with commercial banks. Any deficiency in the pooled cash account is assumed by the general fund and covered through future budgetary appropriation.

Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the Federal Deposit Insurance Corporation (FDIC) coverage. All securities pledged as collateral are held by agents designated by the Commonwealth's Secretary of the Treasury, but not in the Municipality's name.

Cash with fiscal agent in the Debt Service Fund consists of property tax collections and sales and usage taxes amounting to \$9,854,519 that are restricted for the payment of the Municipality's debt service, as required by law. Cash with Fiscal Agent in General Fund consist of \$153,968, in Capital Activities Fund consist principally of \$7,006,932 of unspent proceeds of bonds that are restricted for the acquisition, construction or improvement of major capital assets, and \$13,688 in the Other Governmental Fund. The amounts deposit in GDB is maintained in interest bearing accounts and is not collateralized.

Municipality follows the provisions of GASB Accounting Standards Codification Section C20, *Cash Deposit with Financial Institutions*, related with cash deposit and interest-earning investment contract with financial institutions. Accordingly, the following is essential information about credit risk, interest rate risk, custodial credit risk, and foreign exchange exposure of deposits and investments of the Municipality at June 30, 2013:

Credit Risk

This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2013, the Municipality has invested only in cash equivalents of \$6.6 million consisting of deposit in commercial bank accounts, which are insured by the FDIC, generally up to a maximum of \$250,000. As previously mentioned, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the FDIC coverage. No investments in debt of equity securities were made during the Fiscal Year ended June 30, 2013. Therefore, the Municipality's management has concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2013.

Custodial Credit Risk

This is the risk that, in the event of the failure of a depository financial institution, the Municipality will not be able to recover its cash and investments or will not be able to recover collateral securities that are in the possession of an outside party. Pursuant to the Investment Guidelines for the Commonwealth adopted by GDB, the Municipality may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, banker's acceptance, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. At June 30, 2013, the Municipality has balances deposited in commercial banks amounting to \$6.6 million which are insured by the FDIC up to the established limit and the excess are fully collateralized as explained above. Deposits in GDB, amounting to \$17.0 million are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2013. It is management's policy to only maintain deposits in banks affiliated to FDIC to minimize the custodial credit risk, except for GDB. Therefore, the Municipality's management has concluded that at June 30, 2013, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

continue

3. CASH AND INVESTMENTS – continuation

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 or equity investments in its investments portfolio at June 30, 2013, (2) limiting the weighted average maturity of its investments in certificates of deposit to periods of three months or less, and (3) keeping most of its banks deposits in certificates of deposit and in interest bearing accounts generating interest at prevailing market rates. Therefore, at June 30, 2013, the interest risk associated with the Municipality's cash and cash equivalent is considered low.

Foreign Exchange Risk

This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Municipality, the Municipality is prevented from investing in foreign securities or any other types of investments for 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, 2013.

4. DUE FROM GOVERNMENTAL UNITS

The due from governmental units for the fiscal year ended June 30, 2013 corresponds to \$358,958 from Puerto Rico Treasury Department for the Christmas Bonus and \$273,552 from Municipal Revenue Collection Center for excess of fund retentions.

5. ACCOUNTS AND NOTE RECEIVABLE

Federal Grants

The due from federal grants of the Other Governmental Funds for the fiscal year ended June 30, 2013 corresponds to \$20,269 from the Disaster Grants – Public Assistance Grant, \$275,021 from the Homeland Security Grant Program, \$34,716 from Special Programs for the Aging Title III, \$16,062 from Crime Victim Assistance, \$7,470 from Child and Adult Care Food Program, and \$1,722 from Family Violence Prevention and Services.

Sales and Usage Taxes

Municipality has sales and usage taxes receivable of \$262,610, in the general fund that represents filed tax returns that were uncollected as of June 30, 2013, net of allowance for uncollectible accounts.

Note Receivable

On August 2005, the Municipal Legislature authorized the Mayor to sell the Puerto Rico Distiller for a sale price of \$3,000,000. Of this amount the buyer are paid \$2,090,850. The remaining balance as of June 30, 2013, \$909,150 are claimed by judicial trial. A reserve for uncollectable receivable was made by the Municipality for the total amount of the receivable. The Municipality Legal Division is in charge to collect the amount due.

6. INTERFUND RECEIVABLE, PAYABLES AND TRANSFERS

A. Interfund Receivable and Payable Balances

Due to/from Other Funds at June 30, 2013 are summarized as follows:

Due to	Due From					
	General Fund	Head Start Fund	Debt Service Fund	Capital Activities Fund	Other Governmental Funds	Total Due From
General Fund	\$ -	\$ 393,180	\$ -	\$ 8,721,218	\$ -	\$ 9,114,398
Head Start Fund	-	-	-	333,000	150,000	483,000
Debt Service Fund	-	-	-	-	-	-
Capital Activities Fund	-	-	-	-	-	-
Other Governmental Funds	475,322	-	-	86,720	-	562,042
Total Due To	\$ 475,322	\$ 393,180	\$ -	\$ 9,140,938	\$ 150,000	\$ 10,159,440

B. Interfund Transfers

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

Transfers In	Transfers Out					
	General Fund	Head Start Fund	Debt Service Fund	Capital Activities Fund	Other Governmental Funds	Total Transfer In
General Fund	\$ -	\$ -	\$ -	\$ 169,062	\$ 85,736	\$ 254,798
Head Start Fund	-	-	-	-	-	-
Debt Service Fund	974,000	-	-	-	-	974,000
Capital Activities Fund	-	-	-	-	-	-
Other Governmental Funds	-	-	-	-	-	-
Total Transfer Out	\$ 974,000	\$ -	\$ -	\$ 169,062	\$ 85,736	\$ 1,228,798

Transfer from General Fund to Debt Service Fund are for payment of principal and interest. Transfer from Capital Activities Fund and Other Governmental Funds are for equity transfers other purposes.

continue

7. UNEARNED REVENUES

Government-wide *Statement of Net Position* does not report *deferred inflows of resources*, but report *unearned revenues* for resources receive before it has a legal claim to them. Governmental funds balance sheet report *unearned revenues* in connection with cash collected for revenues that are not considered to be earned in the current period as follows:

Governmental Funds:	
Volume of Business Taxes	\$ 5,702,652
Federal Grants:	
Child and Adult Care Food Program	140,707
ARRA - Head Start Program	3
Family Self Sufficiency	18,247
Special Programs for the Aging - Title III	15,006
Homeless Prevention and Rapid Re-Housing Program	2,531
Emergency Solutions Grant Program	59,751
Urban Development Action Grant Program	50,711
Promoting Safe and Stable Families	1,902
Home Investment Partnerships Program	19,875
Family Violence Prevention and Services	365
ARRA - Child Care and Development Block Gran Program	<u>2,292</u>
Subtotal Federal Grants	<u>6,014,042</u>
State Grants:	
"Manejo de Emergencias" - Defensa Civil	<u>8,655</u>
Total Unearned Revenues	<u>\$ 6,022,697</u>

8. DEFERRED INFLOW OF RESOURCES

Governmental funds balance sheet report *deferred inflows of resources* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period (unavailable). At the end of the current fiscal year, the various components of *deferred inflows of resources* reported in the basic financial statements were as follows:

Governmental Funds:	
Christmas Bonus - Commonwealth	\$ 358,958
Property Taxes - MRCC	832,277
Federal Grants:	
Community Development Block Grant	<u>16,902</u>
Total Deferred Inflows of Resoruces	<u>\$ 1,208,137</u>

9. DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2013, balance due to other governmental units of the General Fund for services rendered to the Municipality, consists of the following:

	AMOUNT
PR Aqueduct and Sewer Authority	\$ 1,621,747
PR Treasury Department	751,065
PR Department of Labor and Human Resources	289,717
Commonwealth of Puerto Rico Employees Association	<u>370,774</u>
Total Due to Governmental Units	<u>\$ 3,033,303</u>

continue

10. CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2013 was as follows:

DESCRIPTION	BALANCE				BALANCE JUNE 30, 2013
	JULY 1, 2012	ADJUSTMENT	INCREASE	DECREASE	
Governmental Activities:					
Non-Depreciable Capital Assets:					
Construction in Progress	\$ 12,886,604	\$ (2,552,561)	\$ 2,480,563	\$ (7,754,668)	\$ 5,059,938
Works of Art	157,261	-	-	-	157,261
Land	54,782,094	2,813,560	-	-	57,595,654
Total Non-Depreciable Capital Assets	<u>67,825,959</u>	<u>260,999</u>	<u>2,480,563</u>	<u>(7,754,668)</u>	<u>62,812,853</u>
Depreciable Capital Assets:					
Buildings	46,464,747	441,000	1,589,315	-	48,495,062
Building Improvements	11,867,269	-	1,347,322	-	13,214,591
Infrastructure	17,017,117	(382,626)	116,094	-	16,750,585
Infrastructure Improvements	9,448,828	-	4,701,937	-	14,150,765
Equipment	5,550,250	-	117,682	(96,921)	5,571,011
Furnitures	1,786,045	-	-	-	1,786,045
Computers	991,892	-	5,545	-	997,437
Motor Vehicles	10,076,734	-	406,845	(42,559)	10,441,020
Total Depreciable Capital Assets	<u>103,202,882</u>	<u>58,374</u>	<u>8,284,740</u>	<u>(139,480)</u>	<u>111,406,516</u>
Less Accumulated Depreciation:					
Buildings	(14,301,574)	(44,100)	(1,209,203)	-	(15,554,877)
Building Improvements	(1,997,710)	-	(328,367)	-	(2,326,077)
Infrastructure	(11,171,640)	92,297	(176,953)	-	(11,256,296)
Infrastructure Improvements	(2,469,510)	-	(749,307)	-	(3,218,817)
Equipment	(4,433,963)	-	(445,345)	96,921	(4,782,387)
Furnitures	(1,681,953)	-	(52,257)	-	(1,734,210)
Computers	(921,541)	-	(66,952)	-	(988,493)
Motor Vehicles	(8,526,384)	-	(624,264)	42,559	(9,108,089)
Works of Art	(145,232)	145,232	-	-	-
Total Accumulated Depreciation	<u>(45,649,507)</u>	<u>193,429</u>	<u>(3,652,648)</u>	<u>139,480</u>	<u>(48,969,246)</u>
Total Depreciable Capital Assets (Net)	<u>57,553,375</u>	<u>251,803</u>	<u>4,632,092</u>	<u>-</u>	<u>62,437,270</u>
CAPITAL ASSETS, NET	<u>\$ 125,379,334</u>	<u>\$ 512,802</u>	<u>\$ 7,112,655</u>	<u>\$ (7,754,668)</u>	<u>\$ 125,250,123</u>

continue

10. CAPITAL ASSETS – continuation

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

	AMOUNT
Governmental Activities:	
Mayor and Municipal Legislature	\$ 386
General Government	692,996
Public Safety	251,569
Public Works	1,079,140
Culture and Recreation	953,211
Human Services and Welfare	18,852
Public Instruction	5,439
Urban Development	651,055
Total Depreciation Expenses	<u>\$ 3,652,648</u>

11. NONCURRENT LIABILITIES

A. General Obligations Bonds and Special Obligations Bonds

The principal long-term obligations of the Municipality are general obligation bonds and special obligation bonds issued to finance the construction and improvements of public facilities and purchase of machinery and equipment. The Municipality's obligations long-term debt retirements are appropriated and paid from resources accumulated in the Debt Service Fund (See Note 12).

The following is a summary of general and special obligation bonds of the Municipality as of June 30, 2013:

Type of Obligation and Purpose	Issue Date	Original Borrowing	Maturity Date	Interest Rate	Balance Amount
General Obligation Bonds:					
Property Taxes Income:					
General Construction	1989	\$ 500,000	2014	5.00%	\$ 40,000
General Construction	1994	400,000	2019	4.87%	159,000
General Construction	1995	14,975,000	2020	4.70% to 6.63%	8,070,000
Operational Expenditures	1998	900,000	2023	4.75%	510,000
General Construction	1999	7,365,000	2024	2.70% to 5.60%	5,110,000
General Construction	2002	5,030,000	2026	2.70% to 5.60%	3,835,000
Operational Expenditures	2003	605,000	2028	1.53% to 6.00%	480,000
Operational Expenditures	2004	360,000	2013	1.53% to 6.00%	45,000
General Construction	2004	1,610,000	2029	1.53% to 6.60%	1,255,000
General Construction	2004	410,000	2019	3.28% to 4.80%	225,000
Operational Expenditures	2005	7,670,000	2014	1.53% to 6.60%	1,850,000
Operational Expenditures	2006	1,056,000	2016	1.53% to 7.00%	510,000
General Construction	2008	1,015,000	2033	1.53% to 7.50%	955,000
General Construction	2009	4,020,000	2033	4.75% to 7.50%	3,750,000
Operational Expenditures	2009	805,000	2024	4.75% to 7.50%	715,000
General Construction	2010	1,355,000	2029	6.00% to 7.50%	1,255,000
Acquisition of Capital Assets	2011	825,000	2017	6.00% to 7.50%	630,000
Operational Expenditures	2012	5,775,000	2018	6.00% to 7.50%	5,120,000
Operational Expenditures	2012	505,000	2037	6.00% to 7.50%	505,000
Total General Obligations Bonds					<u>35,019,000</u>

continue

11. NONCURRENT LIABILITIES – continuation

Type of Obligation and Purpose	Issue Date	Original Borrowing	Maturity Date	Interest Rate	Balance Amount
Special Obligations Bonds:					
General Revenues:					
Operational Ex penditures	2002	10,545,000	2026	1.28% to 8.00%	8,150,000
Operational Ex penditures	2003	4,235,000	2028	6.00%	3,355,000
Operational Ex penditures	2004	294,000	2013	1.53% to 6.62%	36,000
Subtotal					11,541,000
Sales & Usage Taxes:					
Acquisition of Capital Assets	2009	1,845,000	2034	5.00% to 7.50%	1,760,000
Operational Ex penditures	2010	2,095,000	2035	6.00% to 7.50%	2,040,000
Acquisition of Capital Assets	2010	4,140,000	2035	6.50% to 7.00%	4,005,000
Operational Ex penditures	2010	1,228,000	2017	6.00% to 7.50%	939,000
Operational Ex penditures	2011	2,065,000	2036	6.00% to 7.50%	2,040,000
Subtotal					10,784,000
Total Special Obligations Bonds					22,325,000
Total General and Special Obligations Bonds					\$ 57,344,000

During the fiscal year ended June 30, 2013 the Municipality issued general obligation bonds payable in the amount of \$505,000 for operational purposes. Principal and interest on the general obligation bonds are appropriated and paid from resources accumulated in the Debt Service Fund.

Variable interest rates on bonds are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program. Under this program, GDB issues commercial paper: (1) in the taxable and tax-exempt markets of the USA, (2) in the Eurodollar market, and (3) to corporations having tax exemptions under the Puerto Rico Industrial Incentives Acts and, which qualify for benefits provided by the former Section 936 of the US Internal Revenue Code.

According to Sections 103 and 148 through 150 of the US Internal Revenue Code and Sections 1.148 through 1.150 of the US Treasury Regulation, the Municipality's tax-exempt bonds are subject to the arbitrage rebate requirements. At June 30, 2013, the Municipality had no federal arbitrage liability on bonds since interest income earned from the investment of unspent bond proceeds were made in bank deposits that generate yields lower than the rates applicable to the debt service payments.

B. Legal Debt Limit and Legal Debt Margin

On March 9, 2009, the Commonwealth of Puerto Rico approves Law Number 7 that provides for revision of the valuation of property subject to taxation and imposes special property taxes for the Commonwealth. The Municipality debt limits are 10% of valuation of property subject to taxation, plus the balance of the special ad valorem taxes in the Debt Service Fund. 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. Additional legal debt margin was determine for the issuance of the special obligations bonds that are paid through retention made by the MRCC from monthly advance of annual property tax and subsidy send to the Municipality.

C. Other Noncurrent Liabilities

Borrowing from MRCC

On July 1, 2007, the Municipality entered into a repayment agreement with the GDB and MRCC to repay the uncollectible property tax sale authorized by the enacted Law Number 146. The original amount of debt is \$84,149 to be paid during 25 years plus annual interest of 6.22%.

continue

11. NONCURRENT LIABILITIES – continuation

On July 1, 2002, the Municipality entered into a repayment agreement with the GDB and MRCC to repay the uncollectible property tax sale authorized by the enacted Law Number 42. The original amount of debt is \$1,049,742 to be paid during 30 years plus annual interest of 6.1875%.

Landfill Obligation

The Municipality is the current owner of a municipal solid waste landfill consisting of approximately 100 acres, and accounts for certain costs associated with its landfill in accordance with GASB Accounting Standards Codification, Section L10, *Landfill Closure and Post-Closure Care Costs*. Accordingly, the Municipality is required to recognize a liability equal to the estimated total current cost of post-closure care for its landfill. Post-closure care of the Municipality's landfill after its closure is mandated by state and federal laws and consists of various maintenance and monitoring functions at the landfill site. The estimated liability for municipal solid waste landfill closure and post-closure care costs (including monitoring and maintenance) is recorded as a liability in the accompanying GWFS, *Statement of Net Position*.

The estimated total current cost of the landfill closure and post-closure care costs expense during the fiscal year was \$419,258, based on the 63% usage (filled) of the landfill. It is estimated that an additional \$10,707,728 will be recognized between the date of the Statement of Net Position and the expected filled capacity (2032). The estimated total future closure and post-closure care costs (\$28,991,250) 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, 2013. However, due to the nature of closure and post-closure care of municipal landfills, the estimated future costs are subject to annual revision due to changes in applicable regulations, market prices and conditions, and other unforeseeable events.

The Municipality is required to provide financial assurance for the post-closure care activities in accordance with federal regulations, and should identified current and future resources to cover costs relating to the closure and post-closure care costs of the landfill as of June 30, 2013. The Municipality hasn't demonstrates financial assurance to comply with such requirements.

Christmas Bonus

This amount represents the estimated accrued Christmas bonus accumulated as of June 30, 2013 and payroll related benefits, representing the benefit to employees to be paid during the first week of December 2013.

Department of Labor and Human Resources

On June 30, 2013, the Municipality entered into a repayment agreement with the Department of Labor and Human Resources of the Commonwealth of Puerto Rico to repay the unemployment benefit as of June 30, 2013. The repayment agreement is payable in monthly aggregate installments of principals and interest at 8.00% of \$2,238.08. The original amount of debt is \$80,570 under the agreement to be paid during 3 years.

Claims and Judgments

This amount represents the amount accrued for possible claims arising from litigations as recommended by the Municipality's attorneys and classified as due after one year. Only claims is presented as due within one year when the Municipal Legislature approved it in the next fiscal year budget.

Compensated Absences

This amount represents the estimated accrued vacation benefits, accrued sick leave benefits and payroll related benefits, representing the Municipality's commitment to fund such costs from future operations.

continue

11. NONCURRENT LIABILITIES – continuation

Following are the Other Noncurrent Liabilities:

DESCRIPTION	BALANCE JULY 1, 2012	NEW ISSUES	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2013	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER ONE YEAR
Governmental Funds:						
Law Number 42-MRCC	\$ 1,091,562	\$ -	\$ (27,570)	\$ 1,063,992	\$ 29,303	\$ 1,034,689
Law Number 146-MRCC	876,961	-	(43,844)	833,117	43,843	789,274
Landfill Obligation	17,864,264	419,258	-	18,283,522	-	18,283,522
MRCC Liquidation 2011	2,285,407	-	(2,285,407)	-	-	-
MRCC Liquidation 2012	1,347,602	-	-	1,347,602	1,347,602	-
Christmas Bonus	803,093	717,916	(803,093)	717,916	717,916	-
PR Department of Labor	115,619	-	(35,049)	80,570	26,857	53,713
Employees Retirement System	-	2,780,184	-	2,780,184	1,286,976	1,493,208
Claims and Judgments	690,922	5,065,424	-	5,756,346	-	5,756,346
Compensated Absences	5,684,382	-	(622,073)	5,062,309	876,075	4,186,234
TOTAL	\$ 30,759,812	\$ 8,982,782	\$ (3,817,036)	\$ 35,925,558	\$ 4,328,572	\$ 31,596,986

D. Changes in Noncurrent Liabilities

The following is a summary of changes in noncurrent liabilities for the year ended June 30, 2013:

DESCRIPTION	BALANCE JULY 1, 2012	NEW ISSUES	RETIREMENTS AND ADJUSTMENTS	BALANCE JUNE 30, 2013	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER ONE YEAR
Governmental Funds:						
General Obligations Bonds	\$ 37,750,000	\$ 505,000	\$ (3,236,000)	\$ 35,019,000	\$ 3,467,000	\$ 31,552,000
Special Obligations Bonds	22,630,000	-	(305,000)	22,325,000	842,000	21,483,000
Other Obligations	30,759,812	8,982,782	(3,817,036)	35,925,558	4,328,572	31,596,986
TOTAL	\$ 91,139,812	\$ 9,487,782	\$ (7,358,036)	\$ 93,269,558	\$ 8,637,572	\$ 84,631,986

E. Debt Compliance

There are a number of limitations and restrictions contained in the various bond indentures. The Municipality believes it is in compliance with all significant limitations and restrictions.

continue

11. NONCURRENT LIABILITIES – continuation

The annual requirements to amortize the noncurrent liabilities outstanding as of June 30, 2013 are as follows:

YEAR ENDING JUNE 30,	General Obligation Bonds		Special Obligation Bonds		Other Noncurrent Obligations		TOTAL	
	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL	INTEREST
Governmental Funds:								
2014	\$ 3,467,000	\$ 1,750,497	\$ 842,000	\$ 986,879	\$ 4,328,572	\$ 90,666	\$ 8,637,572	\$ 2,828,042
2015	3,609,000	1,933,971	869,000	1,550,025	1,388,820	87,728	5,866,820	3,571,724
2016	2,856,000	1,704,789	927,000	1,483,300	310,033	80,947	4,093,033	3,269,036
2016	3,079,000	1,510,573	996,000	1,411,875	79,025	76,527	4,154,025	2,998,975
2018	3,148,000	1,306,899	1,081,000	1,334,650	81,235	73,219	4,310,235	2,714,768
2019-2023	10,725,000	4,014,190	5,345,000	5,537,033	444,509	311,288	16,514,509	9,862,511
2024-2028	5,210,000	1,731,070	6,670,000	3,179,010	524,759	203,592	12,404,759	5,113,672
2029-2033	2,320,000	613,355	3,250,000	1,432,000	542,502	67,863	6,112,502	2,113,218
2034-2038	605,000	53,063	2,345,000	277,950	-	-	2,950,000	331,013
Unmatured	-	-	-	-	28,226,103	-	28,226,103	-
TOTAL	\$ 35,019,000	\$ 14,618,407	\$ 22,325,000	\$ 17,192,722	\$ 35,925,558	\$ 991,830	\$ 93,269,558	\$ 32,802,959

12. DEBT RETIREMENT

Revenues of the debt service fund consists of the ad-valorem property taxes which are recognized as revenue when collected from taxpayers and reported by the Municipal Revenue Collection Center of the Commonwealth of Puerto Rico (MRCC) to the Municipality (See Note 13).

These property taxes are accumulated by the MRCC in costs of the general obligations bonds issued by the Municipality (See Note 13). Payments are made to the Government Development Bank of the Commonwealth of Puerto Rico from such accumulated funds by the MRCC.

13. PROPERTY TAXES

The Municipality is authorized by Act No. 81 to impose and collect property taxes from any natural or legal person that, at January 1st of each calendar year: (1) is engaged in trade or business and is the owner of personal or real property used in trade or business, or (2) owns residential real property with a value in excess of \$15,000 (at 1957 market price).

The MRCC is responsible for the assessment of all real and personal property located within the Municipality and for the levy, administration and collection of the corresponding tax contribution. Real property taxes are assessed by the MRCC as January 1st of each year.

The personal property tax is self-assessed by the taxpayer on a return, which is to be filed and paid in full by May 15 of each year with the MRCC and based on current values as of December 31 of previous year. Real property tax is assessed by the MRCC on each piece of real estate and on each building or residence. The property tax contribution is levied each year over the appraised value of the real property at the beginning of the calendar year. The real property assessment is based on the current value existing in the year 1957.

The MRCC is responsible for the billing of real property taxes and collections of both, personal and real property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the MRCC informs the Municipality of the estimated amount of property taxes expected to be collected for the ensuing fiscal year. Throughout the year, the MRCC advances funds to the Municipality based on the initial estimated collections. The MRCC 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 MRCC remits to the Municipality property taxes advances, which are less than the tax actually collected, a receivable from the MRCC is recorded at June 30. However, if advances exceed the amount actually collected, a borrowing from MRCC is recorded at June 30. At the time of the preparation of the financial statement, the difference between the advances and the final settlement to the General Fund is pending of final determination.

continue

13. PROPERTY TAXES – continuation

As of June 30, 2013, the CRIM issued the final settlement noting that collections exceeded advances by \$379,167. This balance will be collected from the CRIM during fiscal year 2013-2014. Also, the Municipality owes \$1,347,602 from June 30, 2012 final settlement. This balance will be retained by the CRIM in monthly installments of \$112,300 during fiscal year 2013-2014.

The tax rate for fiscal year 2013 is 10.33% for real property and 8.33% for personal property of which 1.03% of both are for the redemption of public debt issued by the Commonwealth of Puerto Rico and 6.00% and 4.00%, respectively, belongs to the Municipality. Taxpayers pay 10.13% for real property and 8.13% for personal property and the remaining 0.20% is paid by the Commonwealth's Secretary of the Treasury as a subsidy. As part of Act No. 83 of August 30, 1991, as amended, the exempt amount to be paid by the Puerto Rico Secretary of the Treasury to the Municipality was frozen as of January 1, 1992. The remaining percentage is distributed as follows: (a) 6.00% and 4.00%, respectively, represents the Municipality's basic tax rate that is appropriated for general purposes and therefore accounted for through the general fund. 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. The remaining portion belonging to the Municipality of 3.50% represents the ad-valorem property taxes withheld by the MRCC and restricted for debt service, which is accounted for through the debt service fund (See Note 12). The Municipality has reached the maximum statutory tax rate limit for the basic tax while there is no limitation for the ad-valorem tax rate.

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

The Municipality records as revenue in the general fund the property tax contribution when received from monthly advances from MRCC. Due to the fact that collections of property tax are applied to the advances of property tax paid by the MRCC, the amortization of the advance at end of year was not available due to that is in process of verification by external auditors.

The fiscal impact for the future years has not been determined by the Municipality's management.

14. VOLUME OF BUSINESS TAXES

The volume of business taxes is levied each year based on the prior year's gross revenues for all commercial and industrial organizations doing business in the Municipality and which are not totally or partially exempt from this tax under the Industrial Incentives Acts 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 five working days after April 15 of each year. Entities with sales volume of \$3.0 million or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2013, the tax rates were as follows:

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

Taxes are payable in two equal semi-annual installments on July 1 and January 1 following the date of levy. If they are paid with declaration on or before the due date, the taxpayer is granted a 5% of discount. The volume of business tax receivable represents filed tax returns that were uncollected as of June 30, 2013. Collections of taxes during current fiscal year corresponding of the tax return based on the prior year gross sales are applicable to the next fiscal year and recorded as deferred revenues in the General Fund.

15. SALES AND USAGE TAXES

Municipality imposes a Sales and Usage Taxes of 1.5% (1.0% collected and belong to the Municipality and 0.5% collected by the Puerto Rico Secretary of the Treasury) on the sales price of a taxable item or on the purchase price of all usage, storage or consumption of a taxable item. All merchants required to collect the Sales and Usage Taxes, are required to file a monthly Sales and Usage Tax Return Form, no later than the 10th of the following month from the month being reported. The Act also provides for restrictions on the use of the resources (including the 0.5% collected by the Puerto Rico Secretary of Treasury) to be invested in solid waste and recycling programs, capital improvements and health and public safety costs.

continue

15. SALES AND USAGE TAXES – continuation

The amount collected by the Puerto Rico Secretary of Treasury will be deposited in accounts or special funds in GDB, subject to restrictions imposed and distributed as follows:

- a. 0.2% will be deposited in a "Municipal Development Fund" to finance costs as restricted by the Act;
- b. 0.2% will be deposited in a "Municipal Redemption Fund" to finance loans to municipalities subject to restrictions imposed by the Act; and
- c. 0.1% will be deposited in a "Municipal Improvement Fund" to finance capital improvement projects. These funds will be distributed based on legislation from the Commonwealth's Legislature.

Sales and Usage Taxes receivable represents filed sales tax returns that were collected subsequent to June 30, 2013, but pertaining to the current year period.

On February 1, 2014 was enacted the Act Numbers 18 to create the "Law of Municipal Administration Fund (MAF)" and 19 that creates the Municipal Financing Corporation (COFIM by Spanish acronyms). These Acts amend the composition of the SUT effective February 1, 2014 and thereafter. See Note 24 for the changes contemplated by these Acts.

16. CONSTRUCTION EXCISE TAXES

Municipality imposes and collects municipal construction excise taxes to most natural and legal persons and any governmental instrumentality that carry out activities related to construction, expansion, major repairs, relocations, alterations and other types of permanent improvements to residential, commercial and industrial buildings, and any structures within the territorial area of the Municipality. The tax is also applicable to infrastructure projects, the installation of machinery, equipment and fixtures, and other types of construction-related activities.

The construction excise tax generally is a self-assessed tax imposed over the cost of the project, net of certain exemptions such as the costs associated with the acquisition of land, existing buildings and improvements, project design and other engineering fees, licenses and permits, consulting and legal fees. The tax is paid by the taxpayer before the beginning of the construction project.

Any construction project should paid the construction excise taxes as follow:

- a. 2.00% of the total cost of the project for any residential construction; exception: 1.00% for unifamiliar construction by the owner that not is part of a major project. Also, unifamiliar construction with a cost of \$15,000 or less are exempt of tax;
- b. 4.00% of the total cost of the project for any commercial and industrial construction, pavement, repairs, demolitions, streets, highways, bridges, land movement and similar projects;

Taxes are payable before beginning construction or any activity related to the construction. Collections of taxes during current fiscal year, applicable to the next fiscal year, are recorded as deferred revenues in the General Fund.

17. INTERGOVERNMENTAL REVENUES

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

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

continue

18. PENSION PLAN

Defined Benefit Plan

The Government of Puerto Rico Employees Retirement System (ERS) is a cost-sharing multiple-employer defined benefit pension plan sponsored by, and reported as a component unit of, the Commonwealth of Puerto Rico (the Commonwealth). All regular employees of the Municipality under the age of 55 at the date of employment become members of the ERS as a consequence of their employment.

The ERS provides retirement, death, and disability benefits pursuant to Act No. 447, approved on May 15, 1951, as amended, which became effective on January 1, 1952. Disability retirement benefits for occupational and non-occupational disabilities are available to members enrolled in the plan before January 1, 2000. Benefits vest after ten years of plan participation. The amount of the annuity shall be one and one half percent (1.5%) of the average compensation multiplied by the number of years of creditable service up to twenty (20) years, plus two percent (2%) of the average compensation multiplied by the number of years of creditable service in excess of twenty years. In no case shall the annuity be less than \$200 per month.

Participants who have completed at least thirty years of creditable service are entitled to receive a Merit Annuity. Such participants who have not attained fifty-five years of age will receive 65% of the average compensation or if they have attained fifty-five years of age will receive 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten years of service. No benefits are payable if participants receive a refund of their accumulated contributions.

Commonwealth legislation requires that employees hired before April 1, 1990 contribute 5.775% of the first \$550 of their monthly gross salary and 8.275% of their gross monthly salary in excess of \$550. Employees hired after April 1, 1990 contribute 8.275% of their gross monthly salary. The Lottery's contributions are 11.275% of the gross monthly salary.

Defined Contribution Plan

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the ERS, was enacted for the purpose of establishing a new pension program (System 2000). System 2000 became effective on January 1, 2000. Employees participating in the ERS as of December 31, 1999 had the option to stay in the defined benefit plan or transfer to System 2000. Employees joining the Administration on or after January 1, 2000 are only allowed to become members of System 2000.

System 2000 is a defined contribution plan, also known as a cash balance plan. Under this new plan, there is a pool of pension assets, which are invested by the ERS, together with those of the current defined benefit plan. Benefits at retirement age are not guaranteed by the Commonwealth. The annuity is based on a formula that assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) is invested in an account, which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or (2) earn a rate equal to 75% of the return of the ERS' investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances.

System 2000 reduces the retirement age from 65 years to 60 for those employees who joined the ERS on or after April 1, 1990. Disability pensions are not granted under System 2000.

Total employer contributions under both plans during year ended June 30, 2013 amounted to approximately \$2,598,947 which represented 100% of required contributions.

Furthermore, on April 4, 2013, the Governor of Puerto Rico signed into Act No. 3 of 2013, which represents a comprehensive reform of the ERS. Act No. 3 became effective on July 1, 2013 and amends the provisions of the different benefits structures under the ERS, including, but not limited to, the following:

- For active participants of the contributory defined benefit programs under Act No. 447 of 1951 and Act No. 1 of 1990, all retirement benefits accrued through June 30, 2013 will be frozen, and thereafter, all future benefits will accrue under the defined contribution formula used for System 2000 participants, and will be paid at retirement through a lifetime annuity.
- Increases the minimum pension for current retirees from \$400 to \$500 per month.

continue

18. PENSION PLAN – continuation

- The retirement age for Act No. 447 participants will be gradually increased from age 58 to age 61.
- The retirement age for current System 2000 participants is increased gradually from age 60 to age 65.
- Eliminates the “merit annuity” available to participants who joined the ERS prior to April 1, 1990.
- The retirement age for new employees is increased to age 67, except for new state and municipal police officers, firefighters, and custody officers, which will be age 58.
- The employee contribution rate will increase from 8.275% to 10%.
- For System 2000 participants, the retirement benefits will no longer be paid as a lump sum distribution, instead, they will be paid through a lifetime annuity.
- Eliminates or reduces various retirement benefits previously granted by special laws, including Christmas and summer bonuses. The Christmas bonus payable to current retirees is reduced from \$600 to \$200 and is eliminated for future retirees. The summer bonus will be eliminated.
- Disability benefits will be eliminated and substituted for a mandatory disability insurance policy.
- Survivor benefits will be modified.
- The Municipality’s contributions will increase gradually effective July 1, 2013. The required contribution for fiscal year ending June 30, 2014 will be 12.275%. Subsequently the required contribution will increase by 1% every year up to July 1, 2016 when the annual increase will be 1.25% up to a total contribution of 20.525%.

Annual Contribution

The Municipality’s contributions during those years are recognized as total pension expenditures/expenses in the category of administration as follow:

These amounts represented the 100% of the required contribution for the corresponding year. Additionally, changes made in the types and amounts of benefits offered by special laws and costs of living adjustments, led to a one-time recommended contribution to fund the retroactive adjustment related to the changes.

FISCAL YEAR	DEFINED BENEFIT	HYBRID PROGRAM
2013	\$ 209,118	\$ 205,115
2012	812,173	788,262
2011	287,753	490,780

The Employee’s Retirement System of the Government of the Commonwealth of Puerto Rico provides additional information of the Defined Benefit Program and Hybrid Program. They issue a publicly available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Commonwealth. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, PR 00940-2003.

19. HEALTHCARE COSTS

During the year ended June 30, 2000 the Governor of the Commonwealth of Puerto Rico required to the municipalities of Puerto Rico an annual contribution to subsidy the cost of the implementation and administration of the Healthcare Reform. Such contributions are required to be disbursed from general fund operating budget. Total contributions made by the Municipality amounted to approximately \$2,145,456 for the fiscal year ended June 30, 2013.

20. CONTINGENCIES

A. Claims and Judgments

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

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in discovery stage. Certain of these claims are covered by insurance. Legal counsel with the information currently available determine that of these claims the Municipality should reported liabilities of \$5,756,447.

B. Federal Grants

In the normal course of operations, Municipality participates in various federal grant agreements from year to year. The expenditures financed by grants are subject to program compliance audits by the grantor and passed-through agencies in order to assure compliance with grant requirements. If expenditures are disallowed due to noncompliance with grant program regulations, the Municipality may be required to reimburse the grantors for such expenditures.

The Report on Compliance with Requirements Applicable to Each Major Federal Award Program and on Internal Control over Compliance in Accordance with OMB Circular A-133 for the year ended June 30, 2013, disclosed several instances of noncompliance with applicable laws and regulations that were considered to be material weaknesses.

Of the federal expenditures authorized for the fiscal year 2012-2013, the auditors determined that cost amounting \$544,286 are disallowed. Also, \$262,000 of the disallowed costs from prior years are pending of final resolution of the awarding agencies.

Municipality is also subject to audits performed by the Office of the Comptroller of Puerto Rico.

21. COMMITMENTS

A. Operating Leases

The Municipality leases real property, buildings, and equipment under various operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same term. Rental expenditures/expenses recorded in the general fund for the year ended June 30, 2013, amounted to approximately \$105,198. The following is a schedule by years of future minimum rental payments under operating leases that have initial or remaining noncancelable lease with terms exceeding one year as of June 30, 2013:

Year Ending June 30,	Total
2014	\$ 311,108
2015	263,348
2016	256,267
2018	216,367
2018	181,367
After 2018	672,583
Total Minimum Payments	<u>\$ 1,901,040</u>

21. COMMITMENTS – continuation

B. Construction

The Municipality had encumbrances at June 30, 2013 for the construction, improvements, or renovation of several municipal facilities in the following funds:

	Encumbered For	Amount	Reported within Fund Balance Classification
Capital Activities Fund	Improvement of Facilities	\$ 761,607	Restricted to Improvement and Construction of Facilities
	Resurfacing of Streets and other improvements	87,323	Restricted to Improvement of Streets and Sidewalks
	Improvement of Water and Sewer Facilities	1,097,526	Restricted to Improvement of Water and Sewer System

C. Landfill

Landfill Administration

The Municipality has a contract with Landfill Technologies of Arecibo Corp. (LTAC) until June 30, 2018, to provide the service for the operation and administration of the Municipality's landfill. The Municipality shall deposit solid waste at no cost in the landfill by using authorized vehicles of the Municipality. In addition, LTAC is committed to pay the Municipality \$2.00 per ton deposit in the Municipality landfill, except from the Municipality, as royalty, of which \$1.00 should be retained by LTAC for capital improvement on the landfill. On February of 2008, both parts agreed to change the royalty for a recycling program established by LTAC. Also, LTAC is authorized to increase the capacity of the landfill by adding a new cell. When this cell beginning operation, LTAC is committed to pay the Municipality as royalty of 10% of gross revenues.

Solid Waste Disposal Contracts

The Municipality has solid waste disposal contracts with Landfill Technologies of Arecibo Corp. (LTAC) until June 30, 2016, to provide the service for the recollection and disposal of solid waste in the Municipality's landfill. As mentioned above, the Municipality shall deposit solid waste at no cost in the landfill by using authorized vehicles of the Municipality. The contracts provided that the Municipality is committed to pay annually the following amounts. Also, the contracts provide an increase of ten percent (10%) at the third year of service. Expenditure for the year ended June 30, 2013 for this service amounts to \$1.1 million, approximately.

Future commitments are scheduled as follows:

Year	Amount
2014	\$2,365,654
2015	2,474,766
2016	<u>2,590,296</u>
Total	<u>\$7,430,716</u>

D. Financial and Administrative Policies Due to Fiscal Emergency

In Ordinances 28, 37 and 80 approved by the Municipal Legislature on January 15, January 29 and June 12, 2013, respectively, the legislative body authorized the Mayor to establish financial and administrative policies due to fiscal emergency. This Ordinances establish policies of personnel management, awarding of existent and future contracts, equipment acquisition, determining and collecting accounts receivable, legislative body expenditures, use of municipal vehicles, waste management, land disposition, use of facilities fees, sale of advertisement spots, service fees, reduction of legislators fee, and joint ventures with other government agencies and municipalities to provide services.

21. COMMITMENTS – continuation

E. Other Commitments

At June 30, 2013, the other governmental fund had a deficit of \$10,199. The deficits result from the accrual of expenditures without accruing intergovernmental revenues for reimbursement of expenditures. As required by current standards, the Municipality recorded intergovernmental revenues for reimbursement-based (expenditure-driven) grants on GFFS when all applicable eligibility requirements have been met and the resources are available. Any amount not covered by the corresponding award will be covered with future budgetary appropriations of the general fund, if necessary.

22. NET POSITION / FUND BALANCES RESTATEMENTS

A. Net Position

For the year ended June 30, 2013, the Municipality adjusted net position for reclassification, change in accounting principles, and other adjustments to assets, liabilities and revenues.

	GOVERNMENTAL ACTIVITIES
Net Position, as Previously Reported, At June 30, 2012	\$ 40,485,483
Adjustments to Capital Assets	512,802
Adjustments to Long Term Debts	35,051
Adjustments to Fund Balance	2,408,823
Adjustments to Accounts Payable - Construction in Progress	6,129,639
Adjustments to Note Receivable - PR Distillers	(909,150)
Adjustments to Revenue - Christmas Bonus	401,546
Adjustments to Expense - Christmas Bonus	(803,093)
Beginning Net Position, as Restated, At July 1, 2012	<u>\$ 48,261,101</u>

B. Fund Balance

The following reconciles the June 30, 2012 Fund Balance, as previously reported to Beginning Fund Balance, as restated, July 1, 2012 for the various funds:

	GENERAL FUND	SRF HEAD START FUND	CPF STATE & LOCAL GRANTS FUND	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
Fund Balance, as Previously Reported, At June 30, 2012	\$ (17,784,327)	\$ -	\$ 18,260,958	\$ 10,123,610	\$ 1,294,488	\$ 11,894,729
Reclassification of Fund Balances	587,436	-	(587,436)	-	-	-
Adjustment to Account Payable	2,675,370	-	29,358	-	127,154	2,831,882
Reclassification of Fund Balances per GASB 54	535,461	-	-	-	(535,461)	-
Adjustment to Account Payable not Recognized	-	-	(364,485)	(4,678,370)	-	(5,042,855)
Adjustment to Cash	7,720	-	-	-	37,101	44,821
Adjustment to Revenues not Recognized	1,908	-	-	-	395,697	397,605
Beginning Fund Balance, as Restated, At July 1, 2012	<u>\$ (13,976,432)</u>	<u>\$ -</u>	<u>\$ 17,338,395</u>	<u>\$ 5,445,240</u>	<u>\$ 1,318,979</u>	<u>\$ 10,126,182</u>

continue

23. NEW ACCOUNTING STANDARDS

The GASB has issued Statement 61, *The Financial Reporting Entity*. GASB 61 modifies certain requirements for inclusion of component units in the financial reporting entity. For organizations that previously were required to be included as component units by meeting the fiscal dependency criterion, a financial benefit or burden relationship also would need to be present between the primary government and that organization for it to be included in the reporting entity as a component unit. GASB 61 does not have any impact on the Municipality's financial statements.

The GASB has issued Statement 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. GASB 62 incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that are included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the American Institute of Certified Public Accountants (AICPA) Committee on Accounting Procedure. GASB 62 does not have any impact on the Municipality's financial statements.

The Municipality adopted GASB Statement No. 63, *Financial Reporting of Deferred outflows of Resources, Deferred Inflows of Resources, and Net Position* as of June 30, 2013, which changed the Statement of Net Assets to the Statement of Net Position and provides guidance for reporting deferred outflows and inflows of resources. The adoption of this standard did not have any financial impact on the financial statements.

GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions – an amendment of GASB Statement No. 53* was issued in June 2011. The objective of this Statement is to clarify whether an effective hedging relationship continues after the replacement of a swap counterparty or a swap counterparty's credit support provider. This statement sets forth criteria that establish when the effective hedging relationship continues and hedge accounting should continue to be applied. The requirements of Statement No. 64 are effective for financial statements for periods beginning after June 15, 2011 and were adopted the Municipality effective July 1, 2012 with no significant impact on the financial statements.

Also, the Municipality adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* as of June 30, 2013, which establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as revenues and expenses. The adoption of this statement require that debt issuance costs be recognized as an expenses in the period incurred.

24. SUBSEQUENT EVENT

In August 2013 the Municipality entered into an agreement with the Commonwealth of Puerto Rico Retirement System, for the installment payment of its debt, stated as \$2,780,184 as of June 30, 2013 and increased to \$3,860,913 as of the date of the installment payment agreement. The agreement requires 36 monthly installments of \$107,247.53 until the liquidation of the debt.

On September 2013, the Municipality issued general obligation bond of 2013 in the amount of \$3,935,000 for operational expenditures. The principal and interest are payable annually ranging from \$60,000 to \$320,000 through July 2038.

On September 2013, the Municipality authorized the reprogramming of general obligation bond of 2010 for the original amount of \$1,355,000 of which there is a balance of \$1,134,000 to be used for other construction projects.

On October 2013, the Municipality issued general obligation bond of 2013 in the amount of \$4,225,000 for general construction purpose. The principal and interest are payable annually ranging from \$100,000 to \$375,000 through July 2033.

On December 2013, the Municipality authorized the reprogramming of general obligation bond of 2010 for the original amount of \$4,140,000 of which there is a balance of \$500,000 to be used for other construction project.

In addition, on May 2014, the Municipality received the confirmation of an obligation granted by US Department of Agriculture, Rural Development (RD) for the amount of \$211,000 to be used for the acquisition of motor vehicles. The principal and interest are payable annually during 7 years, ranging from \$27,000 to \$34,000 on the 1st days of January of each year through July 2021.

continue

24. SUBSEQUENT EVENT – continuation

As per Act Number 18 of 2014 was created the "Law of Municipal Administration Fund (MAF)" to establish a special fund called the Municipal Administration, authorize municipalities to pledge the funds deposited in the Local Government Fund to which they are to secure the repayment of any loan , bond , note or other evidence of indebtedness , which are the source of repayment funds deposited in the Special Fund and to meet any expenditure budget of the municipality and the municipality any activity or project, authorize the Government Development Bank for Puerto Rico to make disbursements for purposes set out in this Act.

This measure is intended, first, to strengthen the financial capacity of the Corporation Tax Fund of Puerto Rico (COFINA, by Spanish acronyms), established under Law No. 91-2006, as amended, known as the "Law Fund of Sales and Usage Taxes", adjusting the sales and usage taxes (SUT) by increasing the state portion to 6.0% while the municipal SUT is reduced to 1.0%, effective February 1, 2014.

Through this legislation a mechanism under which the SUT collections entitled to receive the Commonwealth of Puerto Rico each fiscal year, after complying with the deposits in the Tax Fund requires by Act No. 91-2006, shall be deposited in a special fund created for the benefit of, and assigned to the municipalities. This special fund is called the "Local Government Fund" ("LGF"), which will be guarded by the Government Development Bank of Puerto Rico.

Also, on February 1, 2014 was enacted the Act No. 19 that creates the Municipal Financing Corporation (COFIM, by Spanish acronyms). The COFIM, attached to the Government Development Bank (GDB), with the power to issue bonds or use other mechanisms to pay or refinance debt incurred by municipalities, the payment of principal and interest is backed by the municipal SUT.

In addition, create the Redemption Fund of COFIM, to which the resources of the existing Municipal Fund Redemption will be transferred effective February 1, 2014, and facilitated the distribution of funds from the Municipal Redemption Fund, the Municipal Development Fund and the Municipal Improvement Fund. Provides that the first proceeds of the municipal SUT of 1% shall be collected by the Treasury Department and deposited directly into the Redemption Fund of COFIM. Provides that bonds and notes issued by the COFIM be payable and secured by the pledge of a fixed amount, or municipal SUT corresponding to a fixed rate of 0.3% has been collected during the previous fiscal year, whichever is greater.

Municipality has evaluated subsequent events through July 30, 2014, the date which the financial statements were available to be issued. Except for the subsequent events mentioned above, no additional events were identified that should be disclosed or adjusted in the Financial Statements or its Notes.

END OF NOTES

REQUIRED SUPPLEMENTARY INFORMATION

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	Budget Amounts		Actual Amounts (Budgetary Basis)	Variance with
	Original	Final	(See Accompanying Notes)	Final Budget
BUDGETARY FUND BALANCE, JULY 1, 2012	\$ (14,601,956)	\$ (14,601,956)	\$ (14,601,956)	\$ -
Resources (Inflows):				
Property Taxes	10,599,053	10,599,053	10,599,053	-
Volume of Business Taxes	9,554,000	9,554,000	6,286,528	(3,267,472)
Sales and Usage Taxes	4,925,000	4,925,000	3,413,925	(1,511,075)
Intergovernmental Revenues	9,555,578	9,555,578	15,288,380	5,732,802
Construction Excise Taxes	7,314,777	7,314,777	1,080,286	(6,234,491)
Rent	175,000	175,000	300,362	125,362
Charges for Services	508,000	508,000	455,716	(52,284)
Miscellaneous	2,093,365	2,093,365	613,778	(1,479,587)
Proceed of Bond	-	505,000	505,000	-
Total Resources (Inflows)	44,724,773	45,229,773	38,543,028	(6,686,745)
Amounts Available for Appropriation	30,122,817	30,627,817	23,941,072	(6,686,745)
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	4,329,669	4,597,527	3,374,906	1,222,621
General Government	18,829,250	19,514,576	23,264,882	(3,750,306)
Public Safety	4,819,000	4,883,998	4,031,561	852,437
Public Works	4,794,067	4,640,944	3,049,303	1,591,641
Culture and Recreation	2,183,444	2,227,129	1,791,816	435,313
Health and Sanitation	1,160,672	1,139,472	1,005,480	133,992
Solid Waste Disposal	3,375,000	3,375,000	1,088,811	2,286,189
Human Services and Welfare	169,568	169,566	92,249	77,317
Public Instruction	2,739,447	2,759,445	1,986,340	773,105
Urban Development	705,696	749,514	397,961	351,553
Capital Outlays	262,500	198,602	79,622	118,980
Transfers to Other Funds	1,356,460	974,000	974,000	-
Total Charges to Appropriations	44,724,773	45,229,773	41,136,931	4,092,842
BUDGETARY FUND BALANCE, JUNE 30, 2013	\$ (14,601,956)	\$ (14,601,956)	\$ (17,195,859)	\$ (2,593,903)

The accompanying Notes to Required Supplementary Information are an integral part of this schedule.

1. **Budgetary Reporting**

The Budgetary Comparison Schedule – General Fund is presented as Required Supplementary Information in accordance with GASB Accounting Standard Codification Section 1700, *The Budget and Budgetary Accounting*. Formal and legal budgetary control is based upon major classes of expenditures known as functions.

2. **Explanation of Differences Between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures**

	<u>General Fund</u>
Sources/Inflows of Resources:	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 60)	\$ 23,941,072
Difference – Budget to GAAP:	
Proceed of Bond	(505,000)
The Fund Balance (Deficit) at the Beginning of Year is a budgetary resource but is not a Current-Year Revenue for financial reporting purposes	<u>14,601,956</u>
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 23)	<u>\$ 38,038,028</u>
Uses/Outflows of Resources:	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 60)	\$ 41,136,931
Difference – Budget to GAAP:	
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(1,175,175)
Payments of encumbrances of prior year that are expenditures for financial reporting purposes but are not outflows for budgetary purposes	701,039
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	<u>(974,000)</u>
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 23)	<u>\$ 39,688,795</u>

END OF THIS SECTION

**SUPPLEMENTARY INFORMATION REQUIRED BY
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**

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SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM –
 FINANCIAL DATA SCHEDULE (RQ020)
 ENTITY WIDE BALANCE SHEET SUMMARY
 JUNE 30, 2013

COMMONWEALTH OF PUERTO RICO
 AUTONOMOUS MUNICIPALITY OF ARECIBO

Submission Type:		Fiscal Year End:
Audited / A-133		June 30, 2013
Assets	Current Assets - Cash:	
111	Cash - Unrestricted	\$ 723,096
113	Cash - Other Restricted	105,367
100	Total Cash	828,463
	Receivables:	
124	Accounts Receivable - Other Government	222,500
128	Fraud Recovery	199,624
128.1	Allowance for Doubtful Accounts - Fraud Recovery	(199,624)
120	Total Receivable, Net of Allowance for Doubtful Accounts	222,500
	Investments:	
131	Investments - Unrestricted	195,956
130	Total Investments	195,956
150	Total Current Assets	1,246,919
	Fixed Assets:	
164	Furniture, Equipment & Machinery - Administration	117,041
166	Accumulated Depreciation	(102,594)
160	Total Capital Assets, Net of Accumulated Depreciation	14,447
190	Total Assets	\$ 1,261,366
Liabilities and Equity	Liabilities:	
	Current Liabilities:	
312	Accounts Payable <=90 days	\$ -
333	Account Payable - Other Government	200,000
347	Inter Program - Due to	-
310	Total Current Liabilities	200,000
300	Total Liabilities	200,000
Equity	Equity	
508.1	Net Investment In Capital Assets	14,447
509.2	Fund Balance Reserved	-
511.1	Restricted Net Position	105,367
512.1	Unrestricted Net Position	941,552
512.2	Unreserved, Undesignated Fund Balance	-
513	Total Equity / Net Position	1,061,366
600	Total Liabilities and Equity / Net Position	\$ 1,261,366

The accompanying Notes to Financial Data Schedule are an integral part of this Supplementary Information.

COMMONWEALTH OF PUERTO RICO
 AUTONOMOUS MUNICIPALITY OF ARECIBO

SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM –
 FINANCIAL DATA SCHEDULE (RQ020)
 PROGRAM REVENUES AND EXPENSES SUMMARY
 FOR THE FISCAL YEAR ENDED JUNE 30, 2013

<u>Submission Type:</u> <u>Audited / A-133</u>	<u>Fiscal Year End:</u> <u>June 30, 2013</u>
70600 HUD PHA Operating Grants	\$ 4,556,761
71100 Investment Income - Unrestricted	1,186
71400 Fraud Recovery	13,244
71500 Other Revenue	<u>65,652</u>
70000 Total Revenue	4,636,843
Expenses:	
Administrative:	
91100 Administrative Salaries	353,504
91500 Employee Benefit Contributions - Administrative	27,043
91900 Other	<u>74</u>
91000 Total Operating - Administrative	380,621
96900 Total Operating Expenses	380,621
97000 Excess of Operating Revenue over Operating Expenses	4,256,222
97300 Housing Assistance Payments	4,120,186
97350 HAP Portability-In	57,904
97400 Depreciation Expense	4,179
97500 Fraud Losses	<u>-</u>
90000 Total Expenses	4,562,890
Excess (Deficiency) of Total Revenue Over (Under) Total	
10000 Expenses	\$ <u>73,953</u>
Memo Account Information:	
11030 Beginning Equity	\$ 987,413
11170 Administrative Fee Equity	\$ 955,999
11180 Housing Assistance Payments Equity	\$ 105,367
11190 Units Months Available	10,436
11210 Number of Units Months Leased	10,396

The accompanying Notes to Financial Data Schedule are an integral part of this Supplementary Information.

1. BASIS OF PRESENTATION

The accompanying Financial Data Schedule (FDS) includes the Section 8 Housing Choice Vouchers Program activities of the Autonomous Municipality of Arecibo (Municipality). The information in the FDS is presented in accordance with the requirements of *HUD's Uniform Financial Reporting Standards for HUD Housing Programs*. Because the FDS presents only a selected portion of the operations of Municipality, it is not intended to and does not present the financial position, or change in net assets of the Municipality.

Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements. The Municipality reporting entity is defined in Note (1) (A) to the basic financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Assets, Liabilities, Net Position, Revenues and Expenses reported on the FDS, are reported on the full accrual basis of accounting. They are recognized following the *HUD's Uniform Financial Reporting Standards for HUD Housing Programs*.

3. RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

Assets, Liabilities and Net Position are presented in the Municipality's Statement of Net Position. Revenues and Expenses are reported in the Statement of Activities.

END OF NOTES

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PART II

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
AND REPORTS REQUIRED BY GOVERNMENT AUDITING
STANDARDS AND OMB CIRCULAR A-133**

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COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FEDERAL GRANTOR / PASS THROUGH GRANTOR / PROGRAM OR CLUSTER TITLE	FEDERAL CFDA NUMBER	PASS-THROUGH ENTITY IDENTIFYING NUMBER	FEDERAL EXPENDITURES
U.S. Department of Agriculture:			
Pass-Through Puerto Rico Department of Education:			
Child and Adult Care Food Program	10.558	CCC-099 CCC-240	\$ 62,853 <u>1,005,338</u>
Total U. S. Department of Agriculture			<u>1,068,191</u>
U.S. Department of Housing and Urban Development:			
Direct Program:			
Community Development Block Grant/Entitlement Grants	14.218		2,092,730
(CDBG).....	14.221		44,689
Urban Development Action Grant Program.....	14.231		96,268
Emergency Solutions Grants Program (ESG).....	14.239		370,080
Home Investment Partnerships Program (HOME).....			
ARRA – Homelessness Prevention and Rapid Re-Housing Program.....	14.257		25,175
Section 8 Housing Choice Vouchers Program.....	14.871		<u>4,558,711</u>
Total U.S. Department of Housing and Urban Development....			<u>7,187,653</u>
U. S. Department of Justice:			
Pass-Through Puerto Rico Department of Justice:			
Crime Victim Assistance.....	16.575	2011-VA-GX-0058	<u>30,860</u>
Total U.S. Department of Justice			<u>30,860</u>
U. S. Department of Transportation:			
Direct Program:			
ARRA – Federal Transit Formula Grants (Urbanized Area Formula Program).....	20.507		<u>376,664</u>
Total U.S. Department of Transportation			<u>376,664</u>
U. S. Environmental Protection Agency (EPA):			
Pass-Through Puerto Rico Environmental Quality Board:			
Capitalization Grants for Clean Water State Revolving Funds ...	66.458	C-72-087-70	<u>411,192</u>
Total U.S. Environmental Protection Agency			<u>411,192</u>
U.S. Department of Health and Human Services:			
Pass-Through Puerto Rico Office for Elderly Affairs:			
Special Programs for the Aging-Title III, Part B-Grants for Supportive Services and Senior Centers (Cluster)	93.044	N/AV	162,291
Special Programs for the Aging-Title III, Part C-Nutrition Service (Cluster).....	93.045	N/AV	204,354
Nutrition Services Incentive Program (Cluster)	93.053	N/AV	<u>50,419</u>
Subtotal Special Programs for the Aging (Cluster)			<u>417,064</u>

continue

**COMMONWEALTH OF PUERTO RICO
AUTONOMOUS MUNICIPALITY OF ARECIBO**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

FEDERAL GRANTOR / PASS THROUGH GRANTOR / PROGRAM OR CLUSTER TITLE	FEDERAL CFDA NUMBER	PASS-THROUGH ENTITY IDENTIFYING NUMBER	FEDERAL EXPENDITURES
Pass-Through Puerto Rico Administration of Families and Children Affairs:			
Promoting Safe and Stable Families	93.556	N/AV	38,512
Family Violence Prevention and Services/Battered Women's Shelters Grants to States and Indian Tribes	93.671	N/AV	<u>75,222</u>
Subtotal Pass-Through Puerto Rico Administration of Families and Children Affairs			<u>113,734</u>
Pass-Through Administration for the Childhood Care and Integral Development:			
Child Care and Development Block Grant	93.575	G01PRCCDF	761,175
Head Start Program.....	93.600	02-CH-9944	<u>10,294,124</u>
Subtotal Pass-Through Administration for the Childhood Care and Integral Development			<u>11,055,299</u>
Total U. S. Department of Health and Human Services.....			<u>11,586,097</u>
U.S. Department of Homeland Security:			
Pass-Through Puerto Rico Office for Public Security:			
Disaster Grants – Public Assistance (Presidentially Declared Disasters).....	97.036	FEMA 1919	<u>50,134</u>
Total U. S. Department of Homeland Security			<u>50,134</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS.....			<u>\$20,710,791</u>

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

1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) includes the federal grant activities of the Autonomous Municipality of Arecibo (Municipality). The information in this Schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of Municipality, it is not intended to and does not present the financial position, or change in net assets of the Municipality.

Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements. The Municipality reporting entity is defined in Note (1) (A) to the basic financial statements. All federal financial awards received directly from federal agency as well as federal financial awards passed-through other government agencies are included on the Schedule.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. Expenditures reported on the Schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State and Local Government*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.
- B. Negative amounts, if any, shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years.
- C. Pass-through entity identifying numbers are presented where available.

3. FEDERAL CFDA NUMBER

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

4. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Expenditures of federal awards are reported in the Municipality's Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Fund as follows: Head Start Fund – \$11,299,462, Capital Activities Fund \$411,192, and Other Governmental Funds \$9,000,137.

END OF NOTES

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INDEPENDENT AUDITOR'S 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
Members of the Municipal Legislature
Autonomous Municipality of Arecibo
Arecibo, Puerto Rico

We have audited, in accordance with the 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, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Autonomous Municipality of Arecibo of the Commonwealth of Puerto Rico (Municipality)**, as of and for the fiscal year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise **Municipality's** basic financial statements, and have issued our qualified report thereon dated July 30, 2014. Our report was qualified because the **Municipality** did not provide a subsidiary of capital assets that agreed with the amounts reported in governmental activities of the Governmental-Wide Financial Statements and, also, the depreciation expense on those assets is not supported.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered **Municipality's** internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of **Municipality's** internal control. Accordingly, we do not express an opinion on the effectiveness of **Municipality's** internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weakness or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the **Municipality's** financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs as items 2013-001 through 2013-007 to be material weaknesses.

INDEPENDENT AUDITOR'S 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
Members of the Municipal Legislature
Autonomous Municipality of Arecibo of the
Commonwealth of Puerto Rico

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the **Municipality's** financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Questioned Costs as items 2013-005 through 2013-007.

Municipality's Response to Findings

Municipality's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. **Municipality's** response was not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the **Municipality's** internal control or on compliance. This report is an integral part of an audit reformed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



CPA Díaz-Martínez, PSC
Certified Public Accountants & Consultants
License Number 12, expires on December 1, 2016

Caguas, Puerto Rico
July 30, 2014

Stamp No. E100094 was affixed to
the original report.





**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE REQUIREMENTS FOR EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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

Report on Compliance for Each Major Federal Program

We have audited **Autonomous Municipality of Arecibo of the Commonwealth of Puerto Rico (Municipality)**'s compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of **Municipality**'s major federal programs for the fiscal year ended June 30, 2013. **Municipality**'s major federal programs are identified in the Summary of Auditor's Result Section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

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

Basis for Qualified Opinion (See the following Table)

As described in the accompanying Schedule of Findings and Questioned Costs, **Municipality** did not comply with requirement regarding the following:

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE REQUIREMENTS FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Honorable Mayor and
 Members of the Municipal Legislature
 Autonomous Municipality of Arecibo of the
 Commonwealth of Puerto Rico

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Finding Number	CFDA Number	Program (or Cluster) Name	Compliance Requirement
2013-008	93.600	Head Start Program	Allowable Costs/Cost Principles
2013-009	10.558; 14.871; 93.600	Child and Adult Care Food Program; Section 8 Housing Choice Vouchers Program; Head Start Program	Allowable Costs/Cost Principles
2013-010	14.218	Community Development Block Grant/Entitlement Grant (CDBG)	Cash Management
2013-011	93.600	Head Start Program	Davis Bacon Act
2013-012	14.871	Section 8 Housing Choice Vouchers Program	Eligibility
2013-013	14.218	Community Development Block Grant/Entitlement Grant (CDBG)	Matching, Level of Effort, and Earmarking
2013-014	ALL	ALL PROGRAMS	Reporting
2013-015	10.558; 14.218; 14.871; 93.575; 93.600	Child and Adult Care Food Program; Community Development Block Grant/Entitlements Grants (CDBG); Section 8 Housing Choice Vouchers Program; Child Care and Development Block Grant Program; Head Start Program	Reporting
2013-016	14.871	Section 8 Housing Choice Vouchers Program	Reporting
2013-017	93.600	Head Start Program	Reporting
2013-018	14.218	Community Development Block Grant/Entitlement Grant (CDBG)	Reporting
2013-019	14.871	Section 8 Housing Choice Vouchers Program	Special Test and Provisions
2013-020	14.871	Section 8 Housing Choice Vouchers Program	Special Test and Provisions

Compliance with such requirements is necessary, in our opinion, for the **Municipality** to comply with the requirements applicable to those programs.

Qualified Opinion (See the above Table)

In our opinion, except for the noncompliance described in the "Basis for Qualified Opinion" paragraph, **Municipality** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the major federal programs described in the above table for the fiscal year ended June 30, 2013.

Other Matters

Municipality's response to the noncompliance finding identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. **Municipality's** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE REQUIREMENTS FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Honorable Mayor and
Members of the Municipal Legislature
Autonomous Municipality of Arecibo

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Report on Internal Control Over Compliance

Management of **Municipality** is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered **Municipality's** internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of **Municipality's** internal control over compliance.

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

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 2013-008 through 2013-020 to be material weaknesses.

Municipality's response to the internal control over compliance finding identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. **Municipality's** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.



CPA Díaz-Martínez, PSC
Certified Public Accountants & Consultants
License Number 12, expires on December 1, 2016

Caguas, Puerto Rico
July 30, 2014

Stamp No. E100095 was affixed to
the original report.



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PART III
FINDINGS AND QUESTIONED COSTS

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SECTION I – SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditors' report issued: Unmodified Opinion
 Modified: Qualified Opinion
 Adverse Opinion
 Disclaimer Opinion

Internal control over financial reporting:

- Material weakness (es) identified? Yes No
- Significant deficiency (ies) identified? Yes None Reported
- Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

- Material weakness (es) identified? Yes No
- Significant deficiency (ies) identified? Yes None Reported

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

- Unmodified Opinion
 Qualified Opinion
- Child and Adult Care Food Program
 - Community Development Block Grants/ Entitlements Grants
 - Section 8 Housing Choice Vouchers Program
 - Child Care and Development Block Grant
 - Head Start Program
- Adverse Opinion Disclaimer Opinion

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

Yes No

Identification of Major Programs:

CFDA Number	Name of Federal Program or Cluster
10.558	Child and Adult Care Food Program
14.218	Community Development Block Grants/ Entitlements Grants
14.871	Section 8 Housing Choice Vouchers Program
93.575	Child Care and Development Block Grant
93.600	Head Start Program

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

\$621,323

Auditee qualified as low-risk auditee?

Yes No

continue

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-001
TYPE OF FINDING	MATERIAL WEAKNESS IN PREPARED FINANCIAL STATEMENTS
CRITERIA	<p>AU Section 325, <i>Communicating Internal Control Related Matters Identified in an Audit</i>, paragraph .15, states the follows:</p> <p>Indicators of material weaknesses in internal control include</p> <p>...</p> <ul style="list-style-type: none">• <u>restatement of previously issued financial statements to reflect the correction of a material misstatement due to error or fraud;</u> <p>...</p> <p>Paragraph 4.23, <i>Communicating Deficiencies in Internal Control, Fraud, Noncompliance with Provisions of Laws, Regulations, Contracts, and Grant Agreements, and Abuse</i>, of the Government Auditing Standards states the follows:</p> <p>4.23 When performing GAGAS financial audits, auditors should communicate in the report on internal control over financial reporting and compliance, based upon the work performed, (1) <u>significant deficiencies and material weaknesses in internal control;</u> ...</p> <p>Paragraph 4.24, <i>Deficiencies in Internal Control</i>, of the Government Auditing Standards states the follows:</p> <p>4.24 The AICPA requirements to communicate in writing significant deficiencies and material weaknesses identified during an audit form the basis for reporting significant deficiencies and material weaknesses in the GAGAS report on internal control over financial reporting when deficiencies are identified during the audit.</p> <p>Appendix I, <i>Supplemental Guidance</i>, paragraph A.06, <i>Examples of Deficiencies in Internal Control</i>, of the Government Auditing Standards states the follows:</p> <p>A.06 The following are examples of control deficiencies:</p> <ul style="list-style-type: none">a. ...b. ...c. <u>Control systems that did not prevent, or detect and correct material misstatements so that it was necessary to restate previously issued financial statements or operational results.</u> Control systems that did not prevent or detect material misstatements in performance or operational results so that it was later necessary to make significant corrections to those results.d. Control systems that did not prevent, or detect and correct material misstatements identified by the auditor. <u>This includes misstatements involving estimation and judgment for which the auditor identifies potential material adjustments and corrections of the recorded amounts.</u>
CONDITION	<p>During the preparation of the financial statements by the Municipality, we noted material misstatements in prior year audited financial statements that required significant adjustments to fund balances/net position. In addition, during our audit of this year financial statements, significant adjustments were proposed to adjust assets, liabilities, revenues, interfund transactions.</p>

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SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-001 – continuation
CAUSE	The Municipality's internal control system, failed to obtain assurance of transactions that affect the financial statements. In addition, the Municipality accounting system does not provide for some mechanized transaction that could lead to errors if proper trace is not maintained.
EFFECT OR POSSIBLE EFFECT	The financial statements for the fiscal year ended June 30, 2013, prepared by the Municipality presented material misstatements related to the beginning balance of the net position/fund balance, and in their assets, liabilities, revenues, interfund transactions.
RECOMMENDATION	We recommend that the Municipality prepare their financial statements using the information from their manual accounting records and Budget Liquidation, and to support the information presented as assets, liabilities, and net position/fund balance for all major and non-major funds.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality will prepare the financial statements for the year ended on June 30, 2014, using the information from the recently implemented electronic accounting system, other subsidiary manual records and Budget Liquidation. The corrective action help to support the information presented as assets, liabilities, and net position/fund balance for all major and non-major funds. In addition, Finance Department had been and is continue to improve its accounting system as well as its accounting policies and procedures to significantly reduce adjustments in the Financial Statements.
IMPLEMENTATION DATE	January 31, 2015
RESPONSIBLE PERSON	Mr. Juan A. Galán Ramirez – Director of Finance

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-002
TYPE OF FINDING	MATERIAL WEAKNESS IN PREPARED FINANCIAL STATEMENTS
CRITERIA	Codification of Governmental Accounting and Financial Reporting Standards, Section 1400.101 states that the reporting entities should report general capital assets in governmental activities, proprietary and fiduciary funds. Capital assets includes land, improvements to land, easements, buildings, building improvements, vehicles, machinery, equipment, works of art and historical treasures, infrastructure, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period (AU § 1400.103). The Municipality should have established internal control policies and procedures in order to properly account for capital assets and to maintain adequate and updated inventory records that provide sufficient and competent evidence to support the existence, rights and obligations, completeness, and valuation and allocation, applicable to the capital assets in governmental activities of the Governmental-Wide Financial Statements.
CONDITION	During our audit the Municipality did not provide a subsidiary of capital assets that agreed with the amounts reported in governmental activities of the Governmental-Wide Financial Statements. Capital assets are the most significant assets of the Municipality and therefore, have a significant impact on the Governmental-Wide Financial Statements.
CAUSE	The Municipality's internal control system, failed to keep track of the additions of capital assets and to assure that the subsidiaries agree with the amounts presented in the Governmental-Wide Financial Statements.
EFFECT OR POSSIBLE EFFECT	The financial statements prepared by the Municipality presented the capital assets and depreciation expense in the Governmental-Wide Financial Statements that do not agree with the subsidiaries provided. In addition, the Governmental-Wide Financial Statements are misstated for an unknown amount related to construction in progress and infrastructure.
RECOMMENDATION	We recommend that the Municipality review the subsidiaries of capital assets in order to assure that they reconcile with the amounts presented in Governmental-Wide Financial Statements. In addition, review all those construction projects that comply with the capitalization policy of the Municipality , and are in progress, and adjust the subsidiaries and Governmental-Wide Financial Statements accordingly.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality will prepare the financial statements for the year ended on June 30, 2014, reviewing the subsidiaries of capital assets in order to assure that they reconcile with the amounts presented in Governmental-Wide Financial Statements. In addition, Finance Department will review of all those construction projects to assure compliance with the capitalization policy of the Municipality , and are in progress, and adjust the subsidiaries and Governmental-Wide Financial Statements accordingly. Completion of this corrective action would take more time than expected due to Municipality's lack of documentation at present time. A special teamwork would be assigned to find the supporting evidence regarding title and ownership of capital assets.
IMPLEMENTATION DATE	June 30, 2015
RESPONSIBLE PERSON	Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-003
TYPE OF FINDING	MATERIAL WEAKNESS
CRITERIA	<p>According to the Law 81, Chapter VI – Administrative Organization, Article 6.003 General Duties for Directors of Administrative Units establish, without this can be understood as a limitation, that the directors of administrative units will have, with respect of them, several duties related to the unit. One of these duties is:</p> <p>(f) Make available to internal auditors, external auditors and the Office of the Comptroller of Puerto Rico, books, files, registers, documents, reports and any other information they request and relevant for the performance of their duties.</p>
CONDITION	<p>During our disbursement internal control test for the general fund, we selected a sample of sixty (60) checks issued, and a total of thirty-seven (37) payments (which included purchase orders, invoices, receiving reports, and other sources documentation) were not available for the performance of our audit procedures.</p> <p>In addition, during our cash receipts internal control test for all funds, we selected a sample of seventy-one (71) transactions, and three (3) cash receipts (which included receipts, deposits slip, cash remittances, and other sources documentation) were not available for the performance of our audit procedures.</p>
CAUSE	<p>The Municipality's internal control system, failed to properly safeguard all documentation related to cash receipts and disbursements.</p>
INFORMATION TO PROVIDE PROPER PERSPECTIVE	<p>Total checks issued selected were 60 (total amount of \$570,739.98), total disbursement checks not available for testing were 37 (total amount of \$452,297.70), this represents 62% of the sample selected.</p> <p>The total cash receipts selected were 71 (total amount of \$9,945,111.84), total cash receipts not available for testing were 3 (total amount of \$217,060.63), this represents 4% of the sample selected.</p>
EFFECT OR POSSIBLE EFFECT	<p>The Municipality may incur in unallowable costs if proper documentation is not submitted for audit procedures.</p>
RECOMMENDATION	<p>We recommend that the Municipality implement internal controls in order to assure that all supporting documentation related to cash receipts and disbursement transactions is properly safeguarded and available for audit procedures.</p>
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	<p>Department of Finance will implement internal controls in order to assure that all supporting documentation related to cash receipts and disbursement transactions is properly safeguarded and available for audit procedures. Specific instructions have been given to Department of Finance employees in order to implement document management and safeguarded procedures.</p>
IMPLEMENTATION DATE	July 31, 2014
RESPONSIBLE PERSON	Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-004
TYPE OF FINDING	MATERIAL WEAKNESS IN PREPARED BANK RECONCILIATIONS
CRITERIA	Chapter VIII, Article 8.010 of Act Number 81 of August 30, 1991, states that the Municipality should maintain an effective and updated accounting system. Section 12 of the Regulations for Municipal Administration states that bank reconciliations for each bank account maintained the municipality must be performed monthly in the Uniform Municipal Accounting System (UMAS). If for some extraordinary reason, they were prevented from using the UMAS, the bank reconciliations are performed in a model in electronic format provided by the Office of the Commissioner of Municipal Affairs. In addition, municipalities have to prepare a monthly report in which the transactions of receipts and disbursements are reflected the month and the balance of funds duly reconciled with the bank reconciliation.
CONDITION	During Fiscal Year 2012-2013, the Municipality failed to prepare bank conciliations for its local, state and federal accounts on a timely manner. Bank conciliations were prepared by an external accounting firm more than a year overdue.
CAUSE	The Municipality did not maintain effective internal control over the transactions recorded on its accounting records and the preparation of its bank conciliations.
EFFECT OR POSSIBLE EFFECT	The Municipality's cash accounting record did not provide updated and complete financial information that presents the correct cash balance in their accounts at the time of authorization of payments.
RECOMMENDATION	We recommend that the Municipality should establish internal control and procedures in order to maintain an accounting system that contains information pertaining to bank reconciliation. The Finance Director will delegate the responsibility to perform the monthly bank reconciliations and reports to an employee or Municipality official under its supervision. These reconciliations should be signed by the employee or officer and must be checked and signed by the Finance Director.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality had established internal control and procedures to maintain the new accounting system with the information pertaining to bank reconciliation. The Director of Finance will delegate the responsibility to perform the monthly bank reconciliations and reports to an employee or Municipality official under its supervision, according to the regulations and legislation, to an external consulting firm or both, according to time schedule and scope of work.
IMPLEMENTATION DATE	July 31, 2014
RESPONSIBLE PERSON	Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-005 (See FINDING REFERENCE NUMBER 2013-013)
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS IN PREPARED SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
CRITERIA	OMB Circular A-102 (Common Rule) Section __.20 Standards for financial management systems states: (a) A State must expand and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds. Fiscal control and accounting procedures of the State, as well as its subgrantees and cost-type contractors, must be sufficient to– (1) Permit preparation of reports required by this part and the statutes authorizing the grant, and (2) Permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes. The Objectives of internal control pertaining to the compliance requirements for Federal programs (Internal Control Over Federal Programs) as found in § __.105 of OMB Circular A-133, includes: Transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and Federal reports.
CONDITION	During our audit procedures of the SEFA prepared by the Municipality we identified material misstatements related to the expenditures presented of all Federal programs. Adjustments were proposed in order to reconcile the information with the financial statements.

continue

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-006 (See FINDING REFERENCE NUMBER 2013-014)
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE – REPORTING PACKAGE OF SINGLE AUDIT
CRITERIA	OMB Circular A-133, Subpart C, Section .320 (a), (c), state all the audit shall be completed and the Data Collection Form and Reporting Package shall be submitted to the Federal Audit Clearinghouse designated by OMB within the earlier of 30 days after receipt of the auditor's report(s), or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audit.
CONDITION	The Municipality did not submit the Data Collection Form and Reporting Package to the Federal Audit Clearinghouse of fiscal year ending June 30, 2013 during the required period.

continue

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-007 (See FINDING REFERENCE NUMBER 2013-015)
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE
CRITERIA	24 CFR Section 5.801 (c) (1) states that the financial information to be submitted to HUD in accordance with paragraph (b) of this section, must be submitted to HUD annually, no later than 60 days after the end of the fiscal year of the reporting period, and as otherwise provided by law. In addition, on Section (d) (1) states that audited financial statements will then be required no later than 9 months after the PHA's fiscal year end, in accordance with the Single Audit Act and OMB Circular A-133.
CONDITION	The Municipality did not submit the required Financial Reports to the US Housing and Urban Development of fiscal year ending June 30, 2013 during the required period. The audited Financial Reports were not submitted on March 31, 2014.

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-008
FEDERAL PROGRAM	HEAD START PROGRAM (93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS-THROUGH PUERTO RICO DEPARTMENT OF FAMILY – ADMINISTRATION FOR THE CHILDHOOD CARE AND INTEGRAL DEVELOPMENT
AWARD NUMBER	241-2012-000193
COMPLIANCE REQUIREMENT	ALLOWABLE COSTS/COST PRINCIPLES
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS
CRITERIA	Circular A-87, Subpart C (1)(j) states that to be allowable under Federal awards, costs must be adequately documented. In addition, Common Rule codified at the Department of Health and Human Services Part 92, Section 92.20 (a)(6) requires that accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and subgrant award documents, etc..
CONDITION	<p>During our audit procedures over Allowable Cost/Cost Principles, we selected a sample of forty (40) checks issued for compliance testing, and five (5) payments were not available for examination.</p> <p>In addition, during our payroll testing, we selected forty (40) employees to ascertain internal controls and compliance over the documentation regarding payroll, and time and attendance records. The Municipality didn't provide evidence of the hours worked for one employee.</p>
QUESTIONED COSTS	Total checks issued not available amounting to \$92,995.83.
INFORMATION TO PROVIDE PROPER PERSPECTIVE	<p>From a population of 850 checks issued, we selected 40 payments, for which 5 checks and related supporting documentation were not available, this represents 13% of the sample selected, or \$92,995.83 in total expenditures.</p> <p>The evidence of the working hours for the payroll ended February 15, 2013 of one employee was not provided.</p>
CAUSE	The Municipality did not maintain an adequate filing system for program disbursements for the fiscal year covered by our audit.
EFFECT OR POSSIBLE EFFECT	Lack of supporting documents could result in unallowable cost that must be reimbursed to the federal agency from state funds.
RECOMMENDATION	We recommend management to develop and implement adequate filing system for program disbursement. In addition, should continue the efforts to locate the missing disbursement documentation.

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-008 – continuation
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality's Department of Finance and Federal programs are developing, establishing and implementing an adequate document management and filing system for program disbursements. Assigned personnel will continue the efforts to locate the missing disbursement documentation and provide the necessary evidence as soon as possible.
IMPLEMENTATION DATE	September 30, 2014
RESPONSIBLE PERSON	Director of Federal Programs and/or Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-009
FEDERAL PROGRAM	CHILD AND ADULT CARE FOOD PROGRAM (CFDA NO. 10.558) U.S. DEPARTMENT OF AGRICULTURE PASS-THROUGH PUERTO RICO DEPARTMENT OF EDUCATION
AWARD NUMBER	CCC-240
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHER PROGRAM (CFDA NO. 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBERS	RQ020
FEDERAL PROGRAM	HEAD START PROGRAM (93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS-THROUGH PUERTO RICO DEPARTMENT OF FAMILY – ADMINISTRATION FOR THE CHILDHOOD CARE AND INTEGRAL DEVELOPMENT
AWARD NUMBER	241-2012-000193
COMPLIANCE REQUIREMENT	ALLOWABLE COSTS/COST PRINCIPLES
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS
CRITERIA	Circular A-87, Subpart C (1)(a) through (h) states that to be allowable under Federal awards, costs must (a) be necessary and reasonable for proper and efficient performance and administration of Federal awards; (b) be allocable to Federal awards under the provisions of this Circular; (c) be authorized or not prohibited under State or local laws or regulations; (d) conform to any limitations or exclusions set forth in these principles, Federal laws, terms and conditions of the Federal award, or other governing regulations as to types or amounts of cost items; (e) be consistent with policies, regulations, and procedures that apply uniformly to both Federal awards and other activities of the governmental unit; (f) be accorded consistent treatment. A cost may not be assigned to a Federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost; (g) except as otherwise provided for in this Circular, be determined in accordance with generally accepted accounting principles; (h) not be included as a cost or used to meet cost sharing or matching requirements of any other Federal award in either the current or a prior period, except as specifically provided by Federal law or regulation.
CONDITION	<p>During our audit procedures over Allowable Cost/Cost Principles of the Head Start Program, we noted that the Municipality transferred to the general bank account of the Municipality the amount of \$200,000 on October 24, 2012; and the amount of \$60,000 on December 18, 2012.</p> <p>In addition, on November 19, 2012, the Municipality transferred the amount of \$200,000 from the Section 8 Housing Choice Voucher Program to the Head Start Program.</p> <p>On December 12, 2012, the Municipality transferred to the general bank account of the Municipality the amount of \$50,000, from the Child and Adult Care Food Program.</p>
QUESTIONED COSTS	\$200,000 from Head Start Program; \$200,000 from Section 8 Housing Choice Vouchers Program, and \$50,000 from Child and Adult Care Food Program.

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-009 – continuation
INFORMATION TO PROVIDE PROPER PERSPECTIVE	<p>On January 4, 2013, the General Fund transferred to the Head Start Program the amount of \$60,000. On February 2013, the Municipality transferred the amount of \$333,000 from other non-federal funds, reported in the Capital Activities Fund, to the Head Start Program.</p> <p>In addition, on November 19, 2012, the Municipality transferred the amount of \$200,000 from the Section 8 Housing Choice Vouchers Program to the Head Start Program. This funds have not been returned to the Section 8 Housing Choice Vouchers Program.</p> <p>On December 12, 2012, the Municipality transferred to the general bank account of the Municipality the amount of \$50,000, from the Child and Adult Care Food Program. This funds have not been returned to the Child and Adult Care Food Program.</p>
CAUSE	The Municipality didn't have adequate internal controls in order to assure that no federal funds are used to support cash flow activities of non-related activities of the federal program.
EFFECT OR POSSIBLE EFFECT	The Municipality incurred in unallowed costs.
RECOMMENDATION	We recommend management to develop and implement adequate internal controls in order to assure that federal funds are used to allowable activities.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management gave specific instructions to the Finance Director and Federal Programs Director to develop and implement adequate internal controls in order to assure that federal funds are used to allowable activities. This situation was assertively attended and is completely corrected.
IMPLEMENTATION DATE	June 30, 2013
RESPONSIBLE PERSON	Director of Federal Programs and/or Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-010
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS/ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBER	B11MC720009
COMPLIANCE REQUIREMENT	CASH MANAGEMENT
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS
CRITERIA	The requirements for cash management are contained in the A-102 Common Rule (§ __.21), OMB Circular A-110 (2 CFR Section 215.22), Treasury regulations at 31 CFR Part 205, program legislation, Federal awarding agency regulations, and the terms and conditions of the award. HUD regulations regarding Community Development Block Grants (CDBG) require that disbursement of funds must occur in a timely manner. While there is no explicit time period, the general rule is that payment must take place within three business days of deposit of CDBG funds. If payment takes longer than three business days, written justification should be maintained in the files.
CONDITION	During our audit procedures over Cash Management requirement, we noted that disbursement of funds after drawdown ranged from four (4) days through twenty-eight (28) days.
QUESTIONED COSTS	None
INFORMATION TO PROVIDE PROPER PERSPECTIVE	From a population of 71 drawdowns made, we selected 10 payments, for which in five (5) drawdowns, disbursements of funds was processed after four (4) through twenty-eight (28) days.
CAUSE	Municipality's Finance Department and program personnel in charge of CDBG program didn't maintain adequate internal controls in order to reduce the time elapsed between the drawdown of funds and subsequent disbursement of funds.
EFFECT OR POSSIBLE EFFECT	This situation may cause that the Municipality might be on a reimbursement basis instead of advance.
RECOMMENDATION	We recommend management to develop and implement adequate internal controls in order to assure that disbursement of funds are made within three business days as required by HUD and Circular A-102.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management has been developed and implemented adequate internal controls in order to assure the disbursement of CDBG funds are made within three (3) business days as required by HUD regulations.
IMPLEMENTATION DATE	June 30, 2014
RESPONSIBLE PERSON	Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-011
FEDERAL PROGRAM	HEAD START PROGRAM (93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS-THROUGH PUERTO RICO DEPARTMENT OF FAMILY – ADMINISTRATION FOR THE CHILDHOOD CARE AND INTEGRAL DEVELOPMENT
AWARD NUMBER	241-2012-000193
COMPLIANCE REQUIREMENT	DAVIS BACON ACT
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS
CRITERIA	45 CFR Section 1309.54 states that Construction and renovation projects and subcontracts financed with funds awarded under the Head Start program are subject to the Davis-Bacon Act (40 U.S.C. 276a et seq.) and the Regulations of the Department of Labor, 29 CFR Part 5. The grantee must provide an assurance that all laborers and mechanics employed by contractors or subcontractors in the construction or renovation of affected Head Start facilities shall be paid wages at not less than those prevailing on similar construction in the locality, as determined by the Secretary of Labor.
CONDITION	The Municipality didn't provide evidence of compliance with the Davis-Bacon Act.
QUESTIONED COSTS	Not Determined.
INFORMATION TO PROVIDE PROPER PERSPECTIVE	The Municipality didn't provide a detail of construction and/or renovation projects financed with Head Start Program funds in order to ascertain compliance with the requirements of the Davis-Bacon Act.
CAUSE	The Municipality did not have a detail of construction and/or renovation projects financed with the Head Start Program.
EFFECT OR POSSIBLE EFFECT	The Municipality can't provide evidence of compliance with payment of prevailing wages rates of construction and/or renovation projects.
RECOMMENDATION	We recommend management to develop and implement internal controls in order to be able to provide details and evidence of compliance of all projects in which Davis-Bacon Act provisions apply.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality's Federal Programs has been implemented internal controls in order to provide details and evidence of compliance of all projects in which Davis-Bacon Act provisions apply. Contractor's certifications and invoices are checked and verified prior to payment process to assure the project document is in compliance with Davis-Bacon provisions.
IMPLEMENTATION DATE	August 30, 2014
RESPONSIBLE PERSON	Director of Federal Programs

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-012
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHER PROGRAM (CFDA NO. 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBERS	RQ020
COMPLIANCE REQUIREMENT	ELIGIBILITY
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE
CRITERIA	24 CFR Section 982.201(a) state that the PHA may admit only eligible families to the program. To be eligible, an applicant must be a "family;" must be income-eligible in accordance with paragraph (b) of this section and 24 CFR Part 5, Subpart F; and must be a citizen or a noncitizen who has eligible immigration status as determined in accordance with 24 CFR Part 5, Subpart E. If the applicant is a victim of domestic violence, dating violence, or stalking, 24 CFR Part 5, Subpart L, applies.
CONDITION	We noted that a new participant was admitted to the program even though that their income exceeded the income guideline established by HUD for a family composition of 4. The Municipality failed to require the participant and other family member's necessary information and documentation to verify income eligibility.
QUESTIONED COSTS	\$1,290
INFORMATION TO PROVIDE PROPER PERSPECTIVE	The Municipality , subsequently noted that the participant was not eligible.
CAUSE	The Municipality program staff failed to perform the required procedures regarding necessary information and documentation to verify income eligibility.
EFFECT OR POSSIBLE EFFECT	The Municipality failed to comply with HUD's regulations regarding the PHA's applicant selection policies. This situation caused unallowable costs related to Section 8 HCV program.
RECOMMENDATION	We recommend management that the Municipality's internal controls should be reviewed in order to improve monitoring of the eligibility determination.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management gave specific instructions to Municipality's Section 8 personnel that internal controls must be reviewed to improve monitoring of the applicant eligibility determination. As a result, the Municipality put in place this corrective action and only eligible participants or families be admitted to the Section 8 Program.
IMPLEMENTATION DATE	June 30, 2014
RESPONSIBLE PERSON	Director of Federal Programs / Section 8 Program Coordinator

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-013
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS/ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBER	B11MC720009
COMPLIANCE REQUIREMENT	MATCHING, LEVEL OF EFFORT, AND EARMARKING
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE
CRITERIA	24 CFR §570.201 (e)(1) establishes that) the amount of CDBG funds used for public services shall not exceed 15 percent of each grant, except that for entitlement grants made under Subpart D of this Part, the amount shall not exceed 15 percent of the grant plus 15 percent of program income, as defined in §570.500(a). For entitlement grants under Subpart D of this Part, compliance is based on limiting the amount of CDBG funds obligated for public service activities in each program year to an amount no greater than 15 percent of the entitlement grant made for that program year plus 15 percent of the program income received during the grantee's immediately preceding program year.
CONDITION	During our audit procedures over earmarking compliance requirement, we found that the Municipality incurred in expenditures amounted to \$246,791.37, according to general ledger, related to public services. According to the formula established by HUD, the limit allowed in public services used, was \$242,209.13.
QUESTIONED COSTS	None
INFORMATION TO PROVIDE PROPER PERSPECTIVE	The total federal grant for fiscal year 2012-2013 was \$1,613,640, plus the program income received during program year, \$1,087.50, totaled \$1,614,727.50. From this amount, the 15 percentage was \$242,209.13. The amount exceed the limit by \$4,582.24, or 0.29%.
CAUSE	Municipality didn't monitored the amounts charged to public services in order to ascertain compliance with the provisions of HUD.
EFFECT OR POSSIBLE EFFECT	This situation may cause the Municipality to have sanctions from HUD, such a reduction of federal assistance.
RECOMMENDATION	We recommend management to develop and implement adequate internal controls in order to assure that expenditures incurred related to public services are monitored during the year to assure compliance.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management has been implemented adequate internal controls to assure the expenditures incurred related to public services are monitored during the year, and assure that not exceed the specific allowable limit according to the formula established by HUD.
IMPLEMENTATION DATE	June 30, 2014
RESPONSIBLE PERSON	Director of Federal Programs

continue

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING REFERENCE NUMBER	2013-014 (See FINDING REFERENCE NUMBER 2013-005)
FEDERAL PROGRAMS	ALL
AWARD NUMBER	(See Schedule of Expenditures of Federal Awards)
COMPLIANCE REQUIREMENT	REPORTING
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS IN PREPARED SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
CRITERIA	OMB Circular A-102 (Common Rule) Section __.20 Standards for financial management systems states: (a) A State must expand and account for grant funds in accordance with State laws and procedures for expending and accounting for its own funds. Fiscal control and accounting procedures of the State, as well as its subgrantees and cost-type contractors, must be sufficient to— (1) Permit preparation of reports required by this part and the statutes authorizing the grant, and (2) Permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes. The Objectives of internal control pertaining to the compliance requirements for Federal programs (Internal Control Over Federal Programs) as found in § __.105 of OMB Circular A-133, includes: Transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and Federal reports.
CONDITION	During our audit procedures of the SEFA prepared by the Municipality we identified material misstatements related to the expenditures presented of all Federal programs. Adjustments were proposed in order to reconcile the information with the financial statements.
QUESTIONED COSTS	None
CAUSE	The SEFA prepared by the Municipality presented expenditures that didn't reconcile with the financial statements. The Municipality used the cash basis of accounting to present the expenditures in the SEFA, but their notes indicated that the modified basis of accounting was used to prepare the SEFA.
EFFECT OR POSSIBLE EFFECT	The Municipality was unable to comply with the submission of some reports due to the fact that the accounting records were not used to reconcile the SEFA with the financial statements.
RECOMMENDATION	We recommend that the Municipality maintain records in order to assure that all expenditures incurred from federal awards are properly incorporated in the SEFA. If the basis of accounting used to prepare the SEFA will be different with the one used to prepare the financial statements, the Municipality should reconcile the differences.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality is maintaining the records and the necessary documentation in order to assure that all expenditures incurred from federal awards are properly incorporated in the SEFA. The Municipality will reconcile any differences if the basis of accounting use to prepare the SEFA would be different with the one used to prepare the financial statements (in such a case).
IMPLEMENTATION DATE	January 31, 2015
RESPONSIBLE PERSON	Director of Federal Programs

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-015 (See FINDING REFERENCE NUMBER 2013-06)
FEDERAL PROGRAM	CHILD AND ADULT CARE FOOD PROGRAM (10.558) U.S. DEPARTMENT OF AGRICULTURE PASS-THROUGH PUERTO RICO DEPARTMENT OF EDUCATION
AWARD NUMBER	0000243865
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS/ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBER	B-12-MC-72-0012
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHER PROGRAM (CFDA NO. 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBER	RQ020
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT PROGRAM (93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS-THROUGH PUERTO RICO DEPARTMENT OF FAMILY – ADMINISTRATION FOR THE CHILDHOOD CARE AND INTEGRAL DEVELOPMENT
AWARD NUMBERS	241-2013-000055-A; 241-2013-000055-B; 241-2013-000055-C
FEDERAL PROGRAM	HEAD START PROGRAM (93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS-THROUGH PUERTO RICO DEPARTMENT OF FAMILY – ADMINISTRATION FOR THE CHILDHOOD CARE AND INTEGRAL DEVELOPMENT
AWARD NUMBERS	241-2012-000176-A; 241-2012-000202
COMPLIANCE REQUIREMENT	REPORTING
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE – REPORTING PACKAGE OF SINGLE AUDIT
CRITERIA	OMB Circular A-133, Subpart C, Section .320 (a), (c), state all the audit shall be completed and the Data Collection Form and Reporting Package shall be submitted to the Federal Audit Clearinghouse designated by OMB within the earlier of 30 days after receipt of the auditor's report(s), or nine months after the end of the audit period, unless a longer period is agreed to in advance by the cognizant or oversight agency for audit.
CONDITION	The Municipality did not submit the Data Collection Form and Reporting Package to the Federal Audit Clearinghouse of fiscal year ending June 30, 2013 during the required period.
QUESTIONED COSTS	None
INFORMATION TO PROVIDE PROPER PERSPECTIVE	The Municipality accounting records did not reconciled with the audited financial statements of prior year. Furthermore, during fiscal year 2012-2013, the Municipality did not have adequate accounting records in order to produce the financial statements with supporting documentation timely.

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-015 (See FINDING REFERENCE NUMBER 2013-006) – continuation
CAUSE	The Municipality were unable to provide timely the financial statements and related supporting documentation in order to apply required audit procedures.
EFFECT OR POSSIBLE EFFECT	The Municipality did not comply with the submission date required for the Data Collection Form and Reporting Package.
RECOMMENDATION	We recommend management to implement adequate internal control procedures in order to assure that accounting records and supporting documentation is available on a timely manner.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management executed administrative actions and implemented adequate internal control procedures into the Finance Department to assure that accounting records and supporting documentation is available on a timely manner. Management goal is that the audit for the year ended on June 30, 2014, will be completed and the Data Collection Form and Reporting Package will be submitted to the Federal Audit Clearinghouse within the earlier of 30 days after receipt of the auditor's report, or the nine months after the end of the audit period.
IMPLEMENTATION DATE	July 31, 2014
RESPONSIBLE PERSON	Director of Federal Programs and/or Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-016 (See FINDING REFERENCE NUMBER 2013-007)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHER PROGRAM (CFDA NO. 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBERS	RQ020
COMPLIANCE REQUIREMENT	REPORTING
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE
CRITERIA	24 CFR Section 5.801 (c) (1) states that the financial information to be submitted to HUD in accordance with paragraph (b) of this section, must be submitted to HUD annually, no later than 60 days after the end of the fiscal year of the reporting period, and as otherwise provided by law. In addition, on Section (d) (1) states that audited financial statements will then be required no later than 9 months after the PHA's fiscal year end, in accordance with the Single Audit Act and OMB Circular A-133. Further, it states that PHAs are required to submit timely GAAP-based unaudited and audited financial information electronically to HUD.
CONDITION	The Municipality did not submit the required Financial Reports to the US Housing and Urban Development of fiscal year ending June 30, 2013 during the required period. The audited Financial Reports were not submitted on March 31, 2014. In addition, the amounts reported in the unaudited financial reports didn't reconcile with accounting records, from which the financial statements of the Municipality were prepared.
QUESTIONED COSTS	None
INFORMATION TO PROVIDE PROPER PERSPECTIVE	The Municipality accounting records did not reconciled with the audited financial statements of prior year. Furthermore, during fiscal year 2012-2013, the Municipality did not have adequate accounting records in order to produce the financial statements with supporting documentation timely.
CAUSE	The Municipality accounting records were not available timely and were not accurate, in order to comply with the required submission dates.
EFFECT OR POSSIBLE EFFECT	The Municipality did not comply with the submission date required for the Financial Reports to the US Housing and Urban Development.
RECOMMENDATION	We recommend management to implement adequate internal control procedures in order to assure that accounting records and supporting documentation is available on a timely manner.

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER 2013-016 (See FINDING REFERENCE NUMBER 2013-007) – continuation

RESPONSIBLE OFFICIAL'S
RESPONSE AND CORRECTIVE
ACTION PLANNED

Management executed administrative actions and implemented adequate internal control procedures into the Finance Department to assure that accounting records and supporting documentation would be available on a timely manner. Management goal is that the audit for the year ended on June 30, 2014, will be completed and the Data Collection Form and Reporting Package will be submitted to the Federal Audit Clearinghouse within the earlier of 30 days after receipt of the auditor's report, or the nine months after the end of the audit period.

IMPLEMENTATION DATE

July 31, 2014

RESPONSIBLE PERSON

Director of Federal Programs and/or
Mr. Juan A. Galán Ramirez – Director of Finance

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-017
FEDERAL PROGRAM	HEAD START PROGRAM (93.600) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS-THROUGH PUERTO RICO DEPARTMENT OF FAMILY – ADMINISTRATION FOR THE CHILDHOOD CARE AND INTEGRAL DEVELOPMENT
AWARD NUMBER	241-2012-000193
COMPLIANCE REQUIREMENT	REPORTING
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS
CRITERIA	According to the Grant Agreement, the program shall submit the Close-Out Report to the Pass-Through Agency not later than 20 calendar days following the close date of the program.
CONDITION	During our Reporting test we noted that the Municipality submitted the Close-Out Report on April 12, 2013, almost thirty-three (33) days after the close of the program year, which is February 28, 2013.
QUESTIONED COSTS	None Noted.
INFORMATION TO PROVIDE PROPER PERSPECTIVE	During fiscal year 2012-2013, the Municipality did not have adequate accounting records in order to produce the financial statements with supporting documentation timely.
CAUSE	The accounting records were not available and complete with the information needed to prepare the reports on a timely basis.
EFFECT OR POSSIBLE EFFECT	This deficiency might lead to a reduction of funds in subsequent years or other administrative sanctions from the Pass-Through Agency.
RECOMMENDATION	We recommend management to implement immediately proper internal controls in order to assure that the accounting records are complete and reconciled.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management executed administrative actions and implemented adequate internal control procedures into the Federal Programs Department and its personnel to assure that all documentation and reports regarding those programs will be available and been submitted to the Pass-Through Agency according to the Grant Agreement.
IMPLEMENTATION DATE	January 31, 2015
RESPONSIBLE PERSON	Director of Federal Programs

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-018
FEDERAL PROGRAMS	COMMUNITY DEVELOPMENT BLOCK GRANTS/ENTITLEMENT GRANTS (CFDA NO. 14.218) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBER	B11MC720009
COMPLIANCE REQUIREMENT	REPORTING
TYPE OF FINDING	MATERIAL NONCOMPLIANCE AND MATERIAL WEAKNESS
CRITERIA	24 CFR, Subpart C, Section 85.41 (b)(4) establishes that HUD requires recipients to submit the FFR (original and two copies), not later than 30 days after the end of each specified reporting period for quarterly and semiannual reports and 90 days for annual reports. Final reports shall be submitted no later than 90 days after the expiration or termination of grant support. In addition, on Section 92.104, establishes that a jurisdiction that has not submitted a consolidated plan to HUD must submit to HUD, not later than 90 days after providing notification under § 92.103, a consolidated plan in accordance with 24 CFR Part 91.
CONDITION	During our Reporting test we noted that the Municipality submitted the Consolidated Annual Performance and Evaluation Report (CAPER) on October 1, 2013, ninety-three (93) days after the end of fiscal year.
QUESTIONED COSTS	None Noted.
INFORMATION TO PROVIDE PROPER PERSPECTIVE	During fiscal year 2012-2013, the Municipality did not have adequate accounting records in order to produce the financial statements with supporting documentation timely.
CAUSE	The accounting records were not available and complete with the information needed to prepare the report on a timely basis.
EFFECT OR POSSIBLE EFFECT	This deficiency might lead to a reduction of funds in subsequent years or other administrative sanctions from the Pass-Through Agency.
RECOMMENDATION	We recommend management to implement immediately proper internal controls in order to assure that the accounting records are complete and reconciled.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Management had been implemented the corrective measures and internal controls to assure that the accounting records are complete and reconciled, in order to submit final reports on time according to regulation.
IMPLEMENTATION DATE	January 31, 2015
RESPONSIBLE PERSON	Director of Federal Programs

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-019
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHER PROGRAM (CFDA NO. 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBERS	RQ020
COMPLIANCE REQUIREMENT	SPECIAL TEST AND PROVISIONS
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE
CRITERIA	24 CFR Section 982.405 (a) states that the PHA must inspect the unit leased to a family prior to the initial term of the lease, at least annually during assisted occupancy, and at other times as needed, to determine if the unit meets the HQS.
CONDITION	During our HQS Inspection Test, we noted that three (3) units were not inspected annually. The lapse of time between the last two periods of inspections fluctuated from twelve days to one and a half months over the required period for the performance of the annual inspection.
QUESTIONED COSTS	None
INFORMATION TO PROVIDE PROPER PERSPECTIVE	A total of 90 participant files were examined; on 3 files examined (3%) we noted that the inspections were made after the required period.
CAUSE	The Municipality didn't have a plan to assure that the visits for the revision of the Housing Quality Standards were made within the required period established by HUD.
EFFECT OR POSSIBLE EFFECT	The Municipality failed to visit the units within the annually time frame required by the regulation. The Municipality did not obtain reasonable assurance that the housing units meet Housing Quality Standards (HQS) established by HUD.
RECOMMENDATION	We recommend management to monitor the performance of the inspections when required, and prepare a schedule of the dates for the visit, in order to assure compliance with this requirement.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Federal Program (Section 8) is in the process of monitoring the performance of the inspections of all units leased under the Program. Management (Federal Programs) had prepared a schedule of the dates for the visit to assure compliance with this requirement.
IMPLEMENTATION DATE	September 30, 2014
RESPONSIBLE PERSON	Director of Federal Programs / Section 8 Coordinator

continue

SECTION III – FINANCIAL STATEMENT FINDINGS

FINDING REFERENCE NUMBER	2013-020
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHER PROGRAM (CFDA NO. 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
AWARD NUMBERS	RQ020
COMPLIANCE REQUIREMENT	SPECIAL TEST AND PROVISIONS
TYPE OF FINDING	MATERIAL WEAKNESS AND MATERIAL NONCOMPLIANCE
CRITERIA	24 CFR Section 982.156 state that unless otherwise required or permitted by HUD, all program receipts must be promptly deposited with a financial institution selected as depository by the PHA in accordance with HUD requirements. The PHA may only withdraw deposited program receipts for use in connection with the program in accordance with HUD requirements. The PHA must enter into an agreement with the depository in the form required by HUD.
CONDITION	The Municipality don't have a signed Depository Agreement form, as required by HUD, with the financial institution during the fiscal year under audit.
QUESTIONED COSTS	None
INFORMATION TO PROVIDE PROPER PERSPECTIVE	Although the depository agreement is not signed, the bank account, where the cash from Section 8 are deposited, is an interest bearing account.
CAUSE	The Municipality fiscal staff failed to obtain the required depository agreement with the bank institution where the program funds are deposited. Also, lack of knowledge of this requirement among the fiscal management prevented the Municipality compliance with this requirement.
EFFECT OR POSSIBLE EFFECT	The Municipality failed to comply with HUD's regulations regarding the depository agreement for the deposit of program funds.
RECOMMENDATION	We recommend management to formalize the required Depository Agreement with the bank where the program funds are being deposited.
RESPONSIBLE OFFICIAL'S RESPONSE AND CORRECTIVE ACTION PLANNED	Municipality will formalize or reviewed the required Depository Agreement with the designated financial institution where the program funds are deposited, in the form required by HUD.
IMPLEMENTATION DATE	September 30, 2014
RESPONSIBLE PERSON	Mr. Juan A. Galán Ramirez – Director of Finance

END OF SCHEDULE

(1) Audit Findings that have been Fully Corrected:

NONE

(2) Audit Findings not Corrected or Partially Corrected:

FISCAL YEAR 2012

Finding Number	12-07	Allowable Costs/Cost Principles Transfer of funds to the Head Start Program.
CFDA Number	10.558	
Questioned Cost	None	
Auditee Comments	Pending of final determination of Pass-Through Entity Puerto Rico Department of Education.	

Finding Number	12-09	Cash Management Delay to disburse requested fund since the date they were received.
CFDA Number	14.218	
Questioned Cost	None	
Auditee Comments	Pending of final determination of US Department of Housing and Urban Development.	

Finding Number	12-10	Reporting Federal Financial Report for the quarter ended March 31, 2012 were not available for examination.
CFDA Number	14.218	
Questioned Cost	None	
Auditee Comments	Pending of final determination of US Department of Housing and Urban Development.	

Finding Number	12-11	Matching, Level of Effort, and Earmarking Municipality has not complied with the use of 70% of funds over a period of up to three years.
CFDA Number	14.218	
Questioned Cost	None	
Auditee Comments	Pending of final determination of US Department of Housing and Urban Development.	

(2) Audit Findings not Corrected or Partially Corrected: – continuation

Finding Number 12-12 **Special Test and Provisions**
 Missing documentation and delay in final inspections relating to
 Housing Rehabilitation.

CFDA Number 14.218

Questioned Cost None

Auditee Comments Pending of final determination of US Department of Housing and Urban Development.

Finding Number 12-15 **Cash Management**
 Delay to disburse requested fund since the date they were received.

CFDA Number 14.257

Questioned Cost None

Auditee Comments Pending of final determination of US Department of Housing and Urban Development.

Finding Number 12-17 **Special Test and Provisions**
 Transfer of funds to the Head Start Program to cover matching funds.
 Also, transfer of funds to the operating account of the General Fund.

CFDA Number 14.871

Questioned Cost None

Auditee Comments Pending of final determination of US Department of Housing and Urban Development.

Finding Number 12-18 **Reporting**
 Audited Financial Statement was not submitted to HUD through the
 REAC in the stipulated date (March 31, 2013).

CFDA Number 14.871

Questioned Cost None

Auditee Comments Pending of final determination of US Department of Housing and Urban Development.

Finding Number 12-20 **Cash Management**
 Delay to disburse requested fund since the date they were received.

CFDA Number 93.575

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the
 Childhood Care and Integral Development of the Puerto Rico Family Department.

continue

(2) Audit Findings not Corrected or Partially Corrected: – continuation

Finding Number 12-21 **Reporting**
 Could not trace the amounts presented in Financial Reports to the accounting records.

CFDA Number 93.575

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

Finding Number 12-22 **Allowable Costs/Cost Principles**
 Count not verify the intended use of transfer of funds to the operating account of the General Fund.

CFDA Number 93.600

Questioned Cost \$210,000

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

Finding Number 12-23 **Cash Management**
 Delay to disburse requested fund since the date they were received.

CFDA Number 93.600

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

Finding Number 12-24 **Allowable Costs/Cost Principles**
 Transfer of funds from the Section 8 Housing Voucher Program to the Head Start Program and from Child and Adult Care Food Program to the Head Start Program.

CFDA Number 10.558
 14.871
 93.575
 93.600

Questioned Cost Not Determinable

Auditee Comments Pending of final determination of Pass-Through Entity PR Administration for Children and Families of the Department of Families, the US Department of Housing and Urban Development, and the Pass-Through Entity Puerto Rico Department of Education.

(2) Audit Findings not Corrected or Partially Corrected: -- continuation

Finding Number	12-25	Procurement, Suspension, and Debarment Missing contract clauses.
CFDA Number	93.600	
Questioned Cost	None	
Auditee Comments	Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.	
Finding Number	12-26	Reporting The Municipality did not complete the single audit for the Fiscal Year 2011-2012 during the period established by the Single Audit Act Amendments of 1996.
CFDA Number	ALL	
Questioned Cost	None	
Auditee Comments	Pending of final determination of the overseeing agency.	
FISCAL YEAR 2011		
Finding Number	11-05	Cash Management Delay to disburse requested fund since the date they were received.
CFDA Number	14.218	
Questioned Cost	None	
Auditee Comments	Pending of final determination of US Department of Housing and Urban Development.	
Finding Number	11-07	Special Test and Provisions Missing documentation and delay in final inspections relating to Housing Rehabilitation.
CFDA Number	14.218	
Questioned Cost	None	
Auditee Comments	Pending of final determination of US Department of Housing and Urban Development.	
Finding Number	11-08	Real Property Acquisition and Relocation Assistance Land acquisition of protected wilderness area that could be preserved in its natural state and could not be developed.
CFDA Number	14.239	
Questioned Cost	\$52,000	
Auditee Comments	Pending of final determination of US Department of Housing and Urban Development.	

continue

(2) Audit Findings not Corrected or Partially Corrected: – continuation

Finding Number 11-10 **Cash Management**
 Delay to disburse requested fund since the date they were received.

CFDA Number 93.575

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

Finding Number 11-11 **Cash Management**
 Delay to disburse requested fund since the date they were received.

CFDA Number 93.600

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

Finding Number 11-13 **Matching, Level Of Effort, and Earmarking**
 The Municipality does not maintain proper documentation to ensure compliance with the program required contribution.

CFDA Number 93.600

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

Finding Number 11-14 **Procurement, Suspension, and Debarment**
 Missing contract clauses.

CFDA Number 93.600

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

FISCAL YEAR 2010

Finding Number 10-15 **Cash Management**
 Delay to disburse requested fund since the date they were received.

CFDA Number 93.575

Questioned Cost None

Auditee Comments Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.

continue

(2) Audit Findings not Corrected or Partially Corrected: – continuation

Finding Number	10-18	Cash Management Delay to disburse requested fund since the date they were received.
CFDA Number	93.600	
Questioned Cost	None	
Auditee Comments	Pending of final determination of Pass-Through Entity Administration for the Childhood Care and Integral Development of the Puerto Rico Family Department.	

(3) Corrective action taken is significantly different from corrective action previously reported:

NONE

(4) Audit findings is no longer valid:

NONE

END OF SCHEDULE