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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

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

FISCAL YEAR ENDED JUNE 30, 2009

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

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

FISCAL YEAR ENDED JUNE 30, 2009

TABLE OF CONTENTS

	Pages
<u>PART I – FINANCIAL:</u>	
Independent Auditors' Report.....	1-2
Required Supplementary Information (Part I): Management's Discussion and Analysis	3-9
<u>BASIC FINANCIAL STATEMENTS:</u>	
Governmental Wide Financial Statements:	
Statement of Net Assets	10
Statement of Activities	11
Governmental Funds Financial Statements:	
Balance Sheet	12
Statement of Revenues, Expenditures and Changes in Fund Balances	13
Reconciliation of the Balance Sheet- Governmental Funds to Statement of Net Assets.....	14
Reconciliation of Statement of Revenues, Expenditures and Changes in Fund Balances to the Statement of Activities	15
Notes to the Basic Financial Statements.....	16-44
Required Supplementary Information:	
Required Supplementary Information (Part II):	
Budgetary Comparison Schedule – General Fund	45
Notes to Budgetary Comparison Schedule – General Fund.....	46
Schedule of expenditures of federal awards.....	47-48
Notes to the schedule of expenditures of federal awards.....	49

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MUNICIPALITY OF ARROYO**

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FISCAL YEAR ENDED JUNE 30, 2009

TABLE OF CONTENTS

INTERNAL CONTROL AND COMPLIANCE WITH LAWS AND REGULATIONS

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..... 50-51

Report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with OMB Circular A-133..... 52-53

FINDINGS AND QUESTIONED COSTS

Schedule of findings and questioned cost..... 54-67

Summary schedule of prior year audit findings..... 68-71



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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

INDEPENDENT AUDITORS' REPORT

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

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

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Arroyo**, Puerto Rico, as of June 30, 2009, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated November 20, 2009, on our consideration of the **Municipality's** internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 3 through 9 and the Budgetary Comparison Schedule-General Fund on pages 45 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

INDEPENDENT AUDITORS' REPORT

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
November 20, 2009

Stamp No. 2407053 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

The management of **Municipality of Arroyo**, Puerto Rico (**Municipality**) offers this narrative overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2009. The Management's Discussion and Analysis (MD&A) is designed to focus on the current year activities, resulting changes and currently known facts, and much of the information is comparable to prior year. This MD&A should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements.

The new reporting model required by Governmental Accounting Standards Board Statement No. 34 was implemented during fiscal 2002-2003. 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:

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

FINANCIAL HIGHLIGHTS

The following are key financial highlights for the fiscal year:

- ❖ The assets of the Municipality exceeded its liabilities at June 30, 2009 by \$19,245,044 and at June 30, 2008 by \$16,376,935, as restated;
- ❖ The Municipality's total net assets increase by \$2,868,109 during fiscal year 2008-2009.
- ❖ As of June 30, 2009, the Municipality's governmental funds reported combined ending fund balances of \$6,793,282, an increase \$4,427,430 from the prior year;
- ❖ At June 30, 2009, the unrestricted deficit was \$9,808,514. During Fiscal Year 2008-2009, the Municipality issue \$4,640,000 in notes debt.
- ❖ The Municipality's capital assets inventory increase as a result of this year's operations. Capital assets as of June 30, 2009 were \$29,078,358, net of depreciation;
- ❖ The investment in capital assets for this year was \$19,757,926, net of related debt;
- ❖ Loans principal payments were \$303,210 and \$287,453 in 2009 and 2008, respectively.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the Municipality's financial statements. The Municipality's basic financial statements comprise three components: government-wide financial statements; fund financial statements; and notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the Municipality's finances, in a manner similar to a private-sector business.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

GOVERNMENT-WIDE FINANCIAL STATEMENTS (CONTINUED)

The Statement of Net Assets presents information on all of the Municipality's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods.

Both of the government-wide financial statements of the Municipality are principally supported by taxes and intergovernmental revenues. The governmental activities of the Municipality include general government, public safety, public works, human services and welfare, culture and recreation, physical environment, education and urban development. Property taxes, municipal license tax, state and federal grants finance most of these activities.

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. The Municipality, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

GOVERNMENTAL FUNDS

The Municipality's basic services are reported in the government fund financial statements. The government funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted into cash. 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. Such information may be useful in evaluating a government's near-term financing requirements. 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, readers may better understand the long-term impact of the government's near-term financing decisions.

The Municipality adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

NOTES TO THE BASIC FINANCIAL STATEMENTS

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

OTHER INFORMATION

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information containing budget to actual comparisons for the general and major funds.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

GOVERNMENT-WIDE FINANCIAL ANALYSIS

GOVERNMENTAL NET ASSETS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Municipality, total assets exceeded liabilities by \$19,245,044 as of June 30, 2009 versus \$16,376,935 as of June 30, 2008, as restated. Our analysis below focuses on the net assets (**Table 1**) and changes in net assets of the Municipality's governmental activities.

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g. land, buildings, machinery and equipment), less any related debt used to acquire those assets still outstanding. These capital assets are used to provide services to citizens; consequently these assets are not available for future spending. It should also be noted that the resources required to repay the related debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Table 1		
Statement of Net Assets	2009	2008
Current and non-current assets	\$ 9,366,748	\$ 5,192,746
Capital assets	<u>29,078,358</u>	<u>26,450,017</u>
Total Assets	<u>38,445,106</u>	<u>31,642,763</u>
Current liabilities	2,593,861	2,558,103
Long-term liabilities	<u>16,606,201</u>	<u>12,707,725</u>
Total Liabilities	<u>19,200,062</u>	<u>15,265,828</u>
Net assets:		
Investment in capital assets	19,757,926	21,516,853
Restricted	9,295,632	5,541,690
Deficit	<u>(9,808,514)</u>	<u>(10,681,608)</u>
Total Net Assets	<u>\$ 19,245,044</u>	<u>\$ 16,376,935</u>

An additional portion of the Municipality's net assets represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets may be used to meet the Municipality's ongoing obligations to citizens and creditors.

Total Net Assets of the Municipality's governmental activities were \$19,245,044. The unrestricted deficit was approximately of \$9,808,514 at June 30, 2009.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

GOVERNMENTAL ACTIVITIES

Governmental activities increased the Municipality's net assets. Key elements of this increase are as follows: the Municipality's governmental activities had net expenses of \$(6,479,898). However, these services are intended to be primarily funded by taxes, as opposed to charges for services and grants, and those taxes and other general revenues exceed net expenses by \$2,868,109. The Municipality expended several of the resources restricted projects in the community.

The cost of all governmental activities this year was \$11,724,134. **Table 2** presents the cost of each of the Municipality's largest programs.

Table 2			
Statement of Activities	2009	2008	
Revenues			
Grants and contributions	\$ 5,069,939	\$ 4,793,407	
General revenues:			
Property taxes	1,413,912	1,709,078	
Municipal license taxes	743,331	725,630	
Municipal sales and use taxes	1,163,072	806,041	
Other local taxes	219,820	479,184	
Grants and contributions not restricted to specific programs	4,966,302	5,037,147	
Interest and investment earnings	138,366	12,254	
Miscellaneous	703,204	214,660	
Charges for services	174,297	181,068	
Total revenues	<u>14,592,243</u>	<u>13,958,469</u>	
Expenses			
General government	4,115,911	4,564,583	
Public safety	379,724	365,746	
Public works	2,859,582	2,558,097	
Health and welfare	2,464,957	2,297,573	
Culture and recreation	398,559	679,092	
Economic development	190,360	150,000	
Community development	875,945	1,183,225	
Interest on long-term debt	439,096	362,582	
Total expenses	<u>11,724,134</u>	<u>12,160,898</u>	
Changes in net assets	2,868,109	1,797,571	
Net assets – beginning, as restated	<u>16,376,935</u>	<u>14,579,364</u>	
Net assets – ending	<u>\$ 19,245,044</u>	<u>\$ 16,376,935</u>	

GOVERNMENT FUND FINANCIAL ANALYSIS

As noted earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

GOVERNMENT FUND FINANCIAL ANALYSIS (CONTINUED)

Table 3			
Balance Sheet	2009	2008	
Assets:			
Total assets – Major Funds	\$ 11,340,275	\$ 7,432,298	
Total assets – Other Funds	<u>1,064,912</u>	<u>896,067</u>	
Combined total assets	<u>12,405,187</u>	<u>8,328,365</u>	
Liabilities:			
Total liabilities – Major Funds	5,335,367	5,827,003	
Total liabilities – Other Funds	<u>276,538</u>	<u>135,510</u>	
Combined total liabilities	<u>5,611,905</u>	<u>5,962,513</u>	
Fund Balances:			
Reserved – Major Funds	8,857,858	5,048,872	
Reserved – Other Funds	788,374	760,557	
Unreserved – Major Funds	<u>(2,852,950)</u>	<u>(3,443,577)</u>	
Combined total fund balances	<u>6,793,282</u>	<u>2,365,852</u>	
Total liabilities and fund balances	<u>\$ 12,405,187</u>	<u>\$ 8,328,365</u>	

Table 4			
Changes in Fund Balances	2009	2008	
Revenues:			
Total revenues – Major Funds	\$ 13,271,109	\$ 12,122,079	
Total revenues – Other Funds	<u>1,583,734</u>	<u>1,617,286</u>	
Combined total revenues	<u>14,854,843</u>	<u>13,739,365</u>	
Expenditures:			
Total expenditures – Major Funds	13,638,794	12,431,057	
Total expenditures – Other Funds	<u>1,428,619</u>	<u>1,394,075</u>	
Combined total expenditures	<u>15,067,413</u>	<u>13,825,132</u>	
Excess of revenues over (expenditures)	<u>(212,570)</u>	<u>(85,767)</u>	
Other financing sources (uses), net:			
Transfers in	307,962	256,778	
Transfers out	(307,962)	(256,778)	
Long-term debt issuance	<u>4,640,000</u>	<u> </u>	
Combined other financing sources (uses), net	<u>4,640,000</u>	<u> </u>	
Net changes in fund balance	<u>4,427,430</u>	<u>(85,767)</u>	
Fund Balance – beginning, as restated	<u>2,365,852</u>	<u>2,451,619</u>	
Fund Balance – ending	<u>\$ 6,793,282</u>	<u>\$ 2,365,852</u>	

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

GOVERNMENTAL FUNDS

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of its fiscal year. At June 30, 2009, the Municipality's governmental funds reported combined ending fund balances of \$6,793,282, an increase of \$4,427,430 from the prior year.

The Municipality has an unreserved fund deficit of \$2,852,950 in its General Fund. The remainder of the balance is reserved to indicate that it is not available for new spending because it has already been committed (1) to liquidate prior year obligations (\$234,401), (2) to pay debt service (\$1,281,361) or (3) for other restricted purposes \$8,130,470.

BUDGETARY HIGHLIGHTS

Budget and actual comparison schedules are provided in the Basic Financial Statements for the General Fund. The Budgetary Comparison Schedule of the General Fund shows the original adopted budgets, the final revised budget, actual results, and variance between the final budget and actual results for the general and major special revenue funds.

After the original budget is approved, it may be revised for a variety of reasons such as unforeseen circumstances and other unanticipated revenues. Differences between the original 2009 budget and the final amended budget for the General Fund were relatively minor and can be summarized as follows:

- ❖ The original budget was amended to increase expenditures between expenditures accounts.

CAPITAL ASSETS AND DEBT ADMINISTRATION

The Municipality's investment in capital assets for its governmental type activities as of June 30, 2009 amounted to \$29,078,358 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, machinery and equipment, parks, roads, highways, and bridges. The total increase in the Municipality's investment in capital assets for the current fiscal year was \$2,628,341. Additions during the fiscal year was principally for building construction, purchase of new vehicles and machinery and equipment, necessary to provides services to our citizens. **Table 5** present the major classes of capital assets, net of accumulated depreciation.

Capital Assets	Amount
Land and construction in progress	\$ 15,699,192
Buildings and buildings improvements	9,575,976
Infrastructure and infrastructure improvements	2,333,775
Equipment, furnishing, works of art and computers	223,941
Vehicles	310,290
Housing Project	935,184
Total Assets	\$ 29,078,358

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

LONG-TERM DEBT

At June 30, 2009 the Municipality had total of \$16,606,201 in general obligations and others outstanding debts, as shown in **Table 6**. Of this amount, \$8,345,000 comprises debt backed by the full faith and credit of the government and \$8,261,201 is other obligations.

Table 6 Long Term Debts	Amount
General obligations	\$ 3,425,000
Special notes	4,920,000
Others	<u>8,261,201</u>
Total Long Term Debts	<u>\$ 16,606,201</u>

The Municipality is required to limit the amount of general obligation debt to 10% of the total assessment of property located within the Municipality in order for the bonds to be repaid with the proceeds of property taxes restricted for debt services. Other obligations include the outstanding balance of a line of credit for construction purposes, accrued vacation and sick leaves, advances of property taxes and landfill closure costs. More detailed information about the Municipality's long-term liabilities is presented in the notes to the financial statements. The Municipality continues to meet its financial needs through prudent use of its revenues and creative debt financing programs.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Local, national and international economic factors influence the Municipality's revenues. Positive economic growth is correlated with increased revenues from property taxes, volume of business taxes, charges for services, as well as state and federal grants. Economic growth in the local economy may be measured by a variety of indicators such as employment growth, unemployment, new construction, assessed valuation, and other revenues.

All of these factors were considered in preparing the Municipality's budget for the 2009 fiscal year. Some cost reductions helped fund improvements of existing facilities, public safety and works, economic development initiatives and human service improvements.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Municipality's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information contact the Municipality's Finance Department at (787) 835-3500.

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

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 4,115,911	\$ -	\$ 103,545	\$ -	\$ (4,012,366)
Public safety	379,724	8,975	120,800		(249,949)
Public works	2,859,582	68,065	15,729	1,197,321	(1,578,467)
Health and welfare	2,464,957		1,824,867		(640,090)
Culture and recreation	398,559	97,257	2,000	847,954	548,652
Economic development	190,360		139,555		(50,805)
Community development	875,945			818,168	(57,777)
Interest on long-term debt	439,096				(439,096)
Total governmental activities	\$ 11,724,134	\$ 174,297	\$ 2,206,496	\$ 2,863,443	\$ (6,479,898)
General revenues:					
					1,413,912
					743,331
					1,163,072
					219,820
					4,966,302
					138,366
					703,204
					<u>9,348,007</u>
					2,868,109
					16,376,935
					<u>\$ 19,245,044</u>

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

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

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 4,115,911	\$ -	\$ 103,545	\$ -	\$ (4,012,366)
Public safety	379,724	8,975	120,800		(249,949)
Public works	2,859,582	68,065	15,729	1,197,321	(1,578,467)
Health and welfare	2,464,957		1,824,867		(640,090)
Culture and recreation	398,559	97,257	2,000	847,954	548,652
Economic development	190,360		139,555		(50,805)
Community development	875,945			818,168	(57,777)
Interest on long-term debt	439,096				(439,096)
Total governmental activities	\$ 11,724,134	\$ 174,297	\$ 2,206,496	\$ 2,863,443	\$ (6,479,898)
General revenues:					
Property taxes					1,413,912
Municipal license taxes					743,331
Municipal sales and use taxes					1,163,072
Other local taxes					219,820
Grants and contributions not restricted to specific programs					4,966,302
Interest and investment earnings					138,366
Miscellaneous					703,204
Total general revenues					9,348,007
Change in net assets					2,868,109
Net assets - beginning-as restated					16,376,935
Net assets - ending					\$ 19,245,044

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

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

	General Fund	Special Revenue Fund - State & Local Grants	Special Revenue Fund Federal Grants	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Assets							
Cash and cash equivalents	\$ -	\$ 885,627	\$ 318,429	\$ 855,565	\$ -	\$ 976,281	\$ 3,035,902
Cash with fiscal agent	37,755		117,370	4,068,612	1,281,361		5,505,098
Accounts receivable:							
Municipal sales and use taxes	59,926						59,926
Intergovernmental	95,804	89,555	242,460	187,953			615,772
Others	29,414					60,646	90,060
Due from other funds	1,046,445	1,973,173	18,331	490			3,038,439
Prepaid expenses	32,005					22,500	54,505
Other assets						5,485	5,485
Total assets	\$ 1,301,349	\$ 2,948,355	\$ 696,590	\$ 5,112,620	\$ 1,281,361	\$ 1,064,912	\$ 12,405,187
Liabilities and Fund Balances							
Liabilities:							
Accounts payable and accrued liabilities	\$ 342,379	\$ -	\$ 191,234	\$ 175,961	\$ -	\$ 78,604	\$ 788,178
Due to other governmental entities	677,729						677,729
Due to other funds	1,973,173	322,878	306,291	238,163		197,934	3,038,439
Deferred revenues:							
Municipal license tax	812,690						812,690
Intergovernmental	95,804						95,804
Federal grant revenues			199,065				199,065
Total liabilities	3,901,775	322,878	696,590	414,124	-	276,538	5,611,905
Fund balances:							
Reserved for:							
Encumbrances	234,401						234,401
Capital projects				4,698,496			4,698,496
Debt service fund					1,281,361		1,281,361
Other purposes	18,123	2,625,477	-				2,643,600
Reserved reported in nonmajor funds:							
Other purposes						788,374	788,374
Unreserved:							
Undesigned	(2,852,950)						(2,852,950)
Total fund balances (deficit)	(2,600,426)	2,625,477	-	4,698,496	1,281,361	788,374	6,793,282
Total liabilities and fund balances	\$ 1,301,349	\$ 2,948,355	\$ 696,590	\$ 5,112,620	\$ 1,281,361	\$ 1,064,912	\$ 12,405,187

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

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

	General Fund	Special Revenue Fund - State & Local Grants	Special Revenue Fund Federal Grants	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Revenues							
Property taxes	\$ 1,365,857	\$ -	\$ -	\$ -	\$ 310,655	\$ -	\$ 1,676,512
Municipal license taxes	743,331						743,331
Municipal sales and use taxes	675,849				487,223		1,163,072
Licenses, permits and other local taxes	219,820						219,820
Intergovernmental	5,069,847	143,567	102,580	1,634,954			6,950,948
Fines and forfeitures	8,975						8,975
Rent of property	97,257					482,355	579,612
Interest	138,366						138,366
Federal grants			1,557,414			1,047,536	2,604,950
Miscellaneous	699,807	15,607				53,843	769,257
Total revenues	9,019,109	159,174	1,659,994	1,634,954	797,878	1,583,734	14,854,843
Expenditures							
Current:							
General government	4,270,194						4,270,194
Public safety	327,938		120,800				448,738
Public works	2,433,506	8,664	426,051	988,739			3,856,960
Health and welfare	599,868	45,860	294,975			1,428,619	2,369,322
Culture and recreation	381,325			2,008,821			2,397,951
Economic development		190,360					190,360
Community development			818,168				818,168
Debt service:							
Principal					303,210		303,210
Interest					412,510		412,510
Total expenditures	8,012,831	252,689	1,659,994	2,997,560	715,720	1,428,619	15,067,413
Excess (deficiency) of revenues over (under) expenditures	1,006,278	(93,515)	-	(1,362,606)	82,158	155,115	(212,570)
Other financing sources (uses)							
Transfers in		50,806			257,156		307,962
Transfers out	(129,241)					(178,721)	(307,962)
Long term debt issuance				4,640,000			4,640,000
Total other financing sources (uses)	(129,241)	50,806	-	4,640,000	257,156	(178,721)	4,640,000
Net change in fund balances	877,037	(42,709)	-	3,277,394	339,314	(23,606)	4,427,430
Fund balance (deficit), beginning-as restated	(3,477,463)	2,668,186	-	1,421,102	942,047	811,980	2,365,852
Fund balance (deficit), ending	\$ (2,600,426)	\$ 2,625,477	\$ -	\$ 4,698,496	\$ 1,281,361	\$ 788,374	\$ 6,793,282

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

Total Fund Balances – Governmental Funds (Page 12)..... \$ 6,793,282

Amounts reported for Governmental Activities in the Statement of Net Assets (Page 8) 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	\$ 15,699,192	
Depreciable Capital Assets	28,473,282	
Accumulated Depreciation	<u>(15,094,116)</u>	
 Total Capital Assets		 29,078,358

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

Municipal Revenue Collection Center	95,804
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Some liabilities are not due and payable in the current period and therefore, are not reported in the funds. Those liabilities consist of:

General Bonds and Notes Payable	8,345,000	
Section 515 Direct Loan	1,950,432	
Compensated Absences	926,092	
Claims and Judgments.....	754,353	
Landfill Obligation	1,567,743	
Property Tax Debt – Law 42	2,206,925	
Property Tax Debt – Law 146	560,968	
Property Tax Debt – Treasury Department	43,231	
LIMS Repayment Plan	76,457	
Puerto Rico Aqueduct and Sewer Authority Debt	<u>175,000</u>	
 Total Long-Term Liabilities.....		 (16,606,201)

Interest liabilities not due and payable in the current period and, therefore, are not reported in the funds..... (116,199)

Total Net Assets of Governmental Activities (Page 10)..... \$ 19,245,044

See accompanying Notes to Basic Financial Statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

Net Change in Fund Balances – Total Governmental Funds (Page 13)		\$ 4,427,430
Amounts reported for Governmental Activities in the Statement of Activities (Page 9) 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 Assets Additions	\$ 3,521,458	
Depreciation Expense.....	<u>(893,117)</u>	
Excess of Capital Assets Additions over Depreciation Expense		2,628,341
Revenues in the statement of activities that not provide current financial resources are not reported as revenue in the funds.....		95,804
Revenues in the governmental funds that correspond to prior year resources are not recorded as revenue in the Statement of Activities		(358,404)
Debt proceeds provide current financial resources to governmental funds, but issuing debt increases long- term liabilities in the Statement of Net Assets. In the current period, these amounts are:		
Notes Payable	<u>4,640,000</u>	
Total Long- Term Debt Issuance		(4,640,000)
Repayments of long-term bonds and notes principal are expenditure in the governmental funds, but the repayment reduces Long–Term Liabilities in the Statement of Net Assets. In the current year the repayments were.....		303,210
Repayments of other long-term debts principal are expenditure in the governmental funds, but the repayment reduces Long–Term Liabilities in the Statement of Net Assets. In the current year the repayments were:		
Decrease in Compensated Absences	285,405	
Increase in Landfill Obligation.....	(61,909)	
Decrease in Property Tax Debt – Law 42.....	42,616	
Decrease in Property Tax Debt – Law 146.....	24,390	
Decrease in Property Tax Debt – Treasury Department.....	43,232	
Decrease in LIMS Repayment Plan.....	27,580	
Decrease in Puerto Rico Aqueduct and Sewer Authority Debt.....	77,000	
Total Additional Expenditures.....		438,314
Certain interest cost reported in the Statement of Activities do not require the use of current financial resources and, therefore are not reported as expenditures in the governmental funds. The following amount represented the change in accrued interest from prior year..		<u>(26,586)</u>
Change in Net Assets of Governmental Activities (Page 11)		<u>\$ 2,868,109</u>

See accompanying Notes to Basic Financial Statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Arroyo**, Puerto Rico (Municipality) was founded in the year 1855, and operates as a governmental unit of the Commonwealth of Puerto Rico, under the Law Number 81 of August 30, 1991, known as "Autonomy Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the Municipality is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of the Commonwealth of Puerto Rico. The legislative body consists of twelve Legislators also elected in the general elections of Puerto Rico for a four-year period.

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

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

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

In June 1999, the GASB issued Statement Number 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*. This statement establishes new financial reporting requirements for state and local governments. The Municipality adopted the provisions of GASBS No. 34, No. 37 and No. 38. They require new information and restructure much of the information that governments have presented in the past.

The accompanying basic financial statements present the financial position and the results of operations of the Municipality and its various funds and fund types, and the cash flows of the proprietary funds. The basic financial statements are presented as of June 30, 2009, and for the fiscal year then ended. The more significant of these accounting policies are described below and, where appropriate, subsequent pronouncements will be referenced.

A. Financial Reporting Entity

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, *The Financial Reporting Entity*, of the GASB, as amended by GASB Statement No. 39. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

A. Financial Reporting Entity (Continued)

A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

B. Measurement Focus and Basis of Accounting

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 the above criteria, the financial statements of Brisas de Arroyo Housing Project no. 565039950 were included in the general-purpose financial statements as a blended component unit.

Blended Component Unit: Brisas de Arroyo Housing Project is a housing development consisting of one hundred four (104) dwelling units located in Arroyo, Puerto Rico. The Project is owned by the Municipality, but the activities on it are carried-on by a management agent unrelated to the Municipality. The housing development is designated to assist various segments of the general public in obtaining adequate and reasonable priced rental housing. The Project operated under financing from US Department of Agriculture Section 515 Rural Rental Housing Loans Program, and with a Section 8 New Construction and Substantial Rehabilitation Program housing assistance grant agreement with US Housing and Urban Development. For financial reporting purposes, the Housing Project is reported as if it were part of the Municipality's operations because its purpose is to provide low-income housing to citizens of the Municipality. The Financial Statements of the blended component unit can be obtained directly from the Municipality's Chief Financial Officer at PO Box 477, Arroyo, Puerto Rico 00714-0477, or call (787) 839-2030.

Government-Wide Financial Statements

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

Governmental Fund Financial Statements

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. Measurement Focus and Basis of Accounting (Continued)

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

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

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

- ❖ Employee's vested annual vacation and sick leave is recorded as expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2009, has been reported only in the government-wide financial statements.

C. Financial Statement Presentation

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

Government-Wide Financial Statements

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

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

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

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

Governmental Fund Financial Statements

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

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

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

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

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

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

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

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

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

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

Special Revenue Fund – Section 8 Voucher Program and Moderate Rehabilitation – Special Revenue Funds are used to account for revenues derived from section 8 choice voucher program and from section 8 moderate rehabilitation program. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund – Housing Project – Special Revenue Funds are used to account for revenues derived from the blended component unit activities. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

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

Capital Projects Fund – State and Local Grants – Capital Projects Fund are used to account for financial resources used for the acquisition or construction of major capital facilities.

Capital Projects Fund – Federal Grants – This is the fund used to account for revenues derived from federal grants related to capital projects. The uses and limitations of each capital projects fund are specified by Municipality ordinances or federal and state statutes.

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

D. Budgetary Data

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Budgetary Data (Continued)

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

1. Prior of May 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 Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law.
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance.
5. If a budget is not adopted prior to the end of the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Municipal Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until a new budget is approved. This permits the Municipality to continue making payments for its operating and other expenses until the new budget is approved.
6. Subsequent to the enactment of the annual appropriation ordinance, the Municipal Legislature has the authority to make necessary amendments made during the fiscal year and are reflected in the budget information included in the Budgetary Comparison Schedule – General Fund.

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

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Budgetary Data (Continued)

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

E. Cash, Cash Equivalent and Investment

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

Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the federal depository insurance generally provided by the Federal Deposit Insurance Corporation (FDIC). 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 represents property tax collections retained by the Municipal Revenues Collection Center and undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico. The sinking fund is maintained by the Governmental Development Bank of Puerto Rico, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

F. Receivables

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

G. Inventories

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

H. Capital Assets

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

H. Capital Assets (Continued)

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

Capital Assets	Years
Buildings and site improvements	40
Infrastructure	40
Works of art	10
Motor vehicles, furniture and fixtures	5
Machinery and equipments	3-5

I. Long-Term Obligations

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

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

J. Compensated Absences

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

J. Compensated Absences (Continued)

The following is a summary of changes in the balance of Compensated Absences for the fiscal year ended June 30, 2009.

<u>BALANCE JULY 1, 2008</u>	<u>NEW ISSUES</u>	<u>RETIREMENTS AND CURRENT MATURATES</u>	<u>BALANCE JUNE 30, 2009</u>	<u>CURRENT PORTION</u>	<u>LONG-TERM PORTION</u>
\$ 1,211,497	\$ _____ -	\$ (285,405)	\$ 926,092	\$ 285,405	\$ 640,687

K. Insurance

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

L. 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 reciprocal and nonreciprocal interfund activities:

- ❖ **Interfund loans** – Represent amounts provided with a requirement for repayment, which are recorded as “due from” in the lender governmental fund and “due to” in the borrower governmental fund. Interfund receivables, which are not considered currently available financial resources, are reported as advances. For amounts not expected to be collected within a reasonable period, interfund receivables/payables are reduced to the estimated realizable value and the amount that is not expected to be repaid is reported as a transfer from the governmental fund that made the loan.
- ❖ **Interfund transfers** – Represent flows of assets (permanent reallocation of financial resources among governmental funds) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as other financing uses in the governmental fund making transfers and as other financing sources in the governmental fund receiving transfers.
- ❖ **Interfund reimbursements** – Represent repayments from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

M. Reservations of Fund Balance – Governmental Funds

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

M. Reservations of Fund Balance – Governmental Funds (Continued)

- ❖ **Capital Projects** – Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
- ❖ **Encumbrances** – Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
- ❖ **Other Purposes** – Represents net assets available for specific use and/or legally segregated for other specific future use.
- ❖ **Debt Service Fund** – Represents net assets available to finance future debt service payments. The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditures or (2) legally segregated for a specific future use. The reserves for related assets such as inventories and prepayments are examples of the former.

N. Claims and Judgments

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

O. Use of Estimates

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

P. Accounting for Pension Costs

For the purpose of applying the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers* (GASB No. 27), the state government of the Commonwealth of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multi-employer cost-sharing defined benefit pension plan and a hybrid defined contribution plan, respectively, 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 of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Commonwealth of Puerto Rico. Accordingly, no portion of the net pension obligation (NPO) related to ERS has been allocated to the Municipality in the accompanying basic financial statements. The basic financial statements of the Commonwealth of Puerto Rico report the total amount of the net pension obligation of ERS, including any amount that may correspond to the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. Accounting for Pension Costs (Continued)

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.

Q. Risk Financing

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

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2009 amounted to \$161,858. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$112,477 for workers compensation insurance covering all municipal employees.

R. Future Adoption of Accounting Pronouncements

The GASB has issued the following accounting standards that have effective dates after June 30, 2009:

- ❖ GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. This Statement is effective for periods beginning after June 15, 2009;
- ❖ GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This statement establishes accounting and reporting requirements for derivative instruments, including hedge accounting. This statement is effective for periods beginning after June 15, 2009;
- ❖ GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. This statement changes the classification and terminology of fund balances and amends the definitions of the different types of governmental funds. This statement is effective for periods beginning after June 15, 2010;
- ❖ GASB Concepts Statements No. 5, *Service Efforts and Accomplishments – an Amendment of GASB Concepts Statements No. 2*. This statement provides a framework to be used by the GASB in considering guidance for reporting SEA by state and local governmental entities and amends terminology and other information in GASB:CS-2. ;

The Municipality's management has concluded that the future adoption of these GASB Statements do not have any impact on the Municipality's basic financial statements.

NOTE 2 – CASH AND CASH EQUIVALENTS

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

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

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

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

Custodial credit risk – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$100,000 per depositor. In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2009. Therefore, the Municipality's management has concluded that at June 30, 2009 the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

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

The Municipality's bank balances in commercial banks of \$885,627 in the special revenue fund – state and local grants, \$318,429 in the special revenue fund – federal grants, and \$855,565 in the capital projects fund – state and local grants, were fully collateralized at June 30, 2009. In the other governmental funds there were deposits with commercial banks of \$976,281 that were fully collateralized.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

The deposits at GDB of \$37,755 in the general fund, the \$117,370 in the special revenue fund – federal grants, the \$4,068,612 in the capital projects fund – state and local grants, and the \$1,281,361 in the debt service fund, are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

NOTE 3 – RECEIVABLES

A. Municipal Sales and Use Taxes Receivable

As described below in Note 14, the Municipal Legislature approved the imposition of the municipal sales and use tax during fiscal year 2006-2007. Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. Tax is due each 20th day of each month based on tax collected in the preceding month. Therefore, sales tax receivable of \$59,926 in the general fund represents the amount due by the taxpayers at June 30, 2009.

B. Intergovernmental Receivables

Intergovernmental receivable in the general fund represents the amounts due from the CRIM resulting from the excess of current year property tax collections over current year advances. Following is a detail of the intergovernmental receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Municipal Revenue Collection Center (CRIM)	\$ 95,804
Total	\$ 95,804

Intergovernmental receivable in special revenue fund – state and local grants represent expenditures incurred not yet reimbursed by a state agency. Following is a detail of the intergovernmental receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Commonwealth of Puerto Rico-Department of Labor and Human Resources	\$ 89,555
Total	\$ 89,555

Intergovernmental receivable in the special revenue fund – federal grants represent expenditures incurred not yet reimbursed by the federal agencies or the pass-through grantors. Following is a detail of the intergovernmental receivable:

<u>Description</u>	<u>Amount</u>
Community Development Block Grant – State's Program	\$ 112,181
Child Care and Development Block Grant	45,006
Disaster Grants – Public Assistance	13,400
Pre-Disaster Mitigation Competitive Grants	57,894
Others	13,979
Total	\$ 242,460

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 3 – RECEIVABLES (CONTINUED)

B. Intergovernmental Receivables (Continued)

Intergovernmental receivable in capital project fund - state and local grants represent expenditures incurred not yet reimbursed by a state agency. Following is a detail of the intergovernmental receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Commonwealth of Puerto Rico – Legislature	\$ 187,953
Total	<u>\$ 187,953</u>

C. Other Receivables

Other receivable of \$29,414 in the general fund represents accounts receivables at June 30, 2009, related to landfill royalties. In addition, other receivable of \$60,646 in other governmental funds represents accounts receivables at June 30, 2009, relates to the blended component unit housing project.

NOTE 4 – INTERFUND TRANSFER AND BALANCES

A. INTERFUND RECEIVABLES – DUE FROM / TO OTHER FUNDS

Interfund receivables and payables at June 30, 2009 are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund– Local and State Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	\$ 304,057
General Fund	Special Revenue Fund– Federal Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	306,291
General Fund	Capital Projects Fund– Local and State Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	238,163
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed	197,934
Special Revenue Fund– Local and State Grants	General Fund	Cash pool in the same bank account and other reimbursable expenditures	1,973,173
Special Revenue Fund– Federal Grants	Special Revenue Fund– Local and State Grants	Reimbursable expenditures	18,331
Capital Projects Fund– Local and State Grants	Special Revenue Fund– Local and State Grants	Reimbursable expenditures	<u>490</u>
Total			<u>\$ 3,038,439</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 5 – CAPITAL ASSETS

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

Governmental Activities	Balance July 1, 2008	Additions	Retirements / Reclassifications	Balance June 1, 2009
Capital asset, not being depreciated:				
Land	\$ 9,705,674	\$ -	\$ -	\$ 9,705,674
Construction in progress	5,021,055	1,626,996	(1,249,533)	5,398,518
Housing Project	595,000	-	-	595,000
Total capital assets not being depreciated	<u>15,321,729</u>	<u>1,626,996</u>	<u>(1,249,533)</u>	<u>15,699,192</u>
Capital assets, being depreciated:				
Buildings	13,557,545	130,033		13,687,578
Building improvements	811,284	2,065,263		2,876,547
Infrastructure	3,407,338	298,825		3,706,163
Infrastructure improvements	746,958	415,500		1,162,458
Equipment	640,391	151,783		792,174
Furnishing	316,836			316,836
Work of Art	3,410			3,410
Computers	84,517	8,039		92,556
Vehicles	2,107,062	61,290		2,168,352
Housing Project – depreciable assets	3,653,946	13,262	-	3,667,208
Total capital assets being depreciated	<u>25,329,287</u>	<u>3,143,995</u>	<u>-</u>	<u>28,473,282</u>
Less accumulated depreciation for:				
Buildings	(6,491,032)	(341,420)		(6,832,452)
Building improvements	(73,559)	(82,138)		(155,697)
Infrastructure	(2,205,647)	(89,846)		(2,295,493)
Infrastructure improvements	(192,156)	(47,197)		(239,353)
Equipment	(523,205)	(71,983)		(595,188)
Furnishing	(292,381)	(9,843)		(302,224)
Work of Art	(1,932)	(341)		(2,273)
Computers	(72,461)	(8,889)		(81,350)
Vehicles	(1,724,679)	(133,383)		(1,858,062)
Housing Project – depreciable assets	(2,623,947)	(108,077)	-	(2,732,024)
Total accumulated depreciation	<u>(14,200,999)</u>	<u>(893,117)</u>	<u>-</u>	<u>(15,094,116)</u>
Total capital assets being depreciated, net	<u>11,128,288</u>	<u>2,250,878</u>	<u>-</u>	<u>13,379,166</u>
Governmental activities capital assets, net	<u>\$ 26,450,017</u>	<u>\$ 3,877,874</u>	<u>\$ (1,249,533)</u>	<u>\$ 29,078,358</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 5 – CAPITAL ASSETS (CONTINUED)

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

Governmental activities	Amount
General government	\$ 311,241
Public Safety	52,343
Public Works	185,352
Community Development	57,777
Health and Welfare	111,262
Culture and Recreation	<u>175,142</u>
Total depreciation expenses	<u>\$ 893,117</u>

The infrastructure assets recorded in the accompanying statement of net assets do not include a substantial portion of the Municipality's infrastructure assets constructed or acquired by the Municipality from 1980 through June 30, 2007. GASB Statement No. 34 requires to retroactively apply the requirements to major general infrastructure assets within at least four (4) years of the adoption of this pronouncement, which is not later than June 30, 2007. The Municipality complied with this requirement.

NOTE 6 – ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities in governmental fund financial statements represent expenditures incurred during fiscal year 2008-2009, and not paid by the Municipality at June 30, 2009. Following is a detail of these accounts payable and accrued liabilities:

Major Governmental Funds	Accounts Payable	Accrued Liabilities	Total
General Fund	\$ 84,507	\$ 257,872	\$ 342,379
Special Revenue Fund – Federal Grants	191,234		191,234
Capital Projects Fund – State & Local Grants	175,961		175,961
Other Governmental Funds	<u>78,604</u>	<u>-</u>	<u>78,604</u>
Total	<u>\$ 530,306</u>	<u>\$ 257,872</u>	<u>\$ 788,178</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 7 – DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2009, balance due to other governmental units consists of the following:

<u>Governmental Agency</u>	<u>Amount</u>
Puerto Rico Aqueduct and Sewer Authority	\$ 115,722
General Service Administration	10,302
Treasury Department	519,666
Department of Labor	30,414
Puerto Rico Electric Power Authority (PREPA)	<u>1,625</u>
Total	<u>\$ 677,729</u>

NOTE 8 – DEFERRED REVENUES

- A. Municipal License Tax** – The deferred revenues of \$812,690 in the general fund relates to municipal license tax collected in fiscal year 2008-09 that will be earned in fiscal year 2009-10.
- B. Intergovernmental** – The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the final liquidation noting that the collections exceeded advances by \$95,804. In the governmental funds, the entire receivable has been offset by deferred revenue since the excess was not available to pay liabilities of the current period. In the government-wide financial statements, the entire receivable is recognized as revenue.
- C. Federal Government** – The deferred revenues presented in the special revenue fund – federal grants represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Emergency Management Performance Grant	\$ 34,470
Disaster Grants – Public Assistance	108,299
Child Care and Development Block Grant	44,880
Others	<u>11,416</u>
Total	<u>\$ 199,065</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 9 – GENERAL LONG-TERM DEBTS

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

Description	Beginning Balance	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds Payable	\$ 3,630,000	\$ -	\$ (205,000)	\$ 3,425,000	\$ 230,000
Note Payable	343,000	4,640,000	(63,000)	4,920,000	135,000
Section 515 direct loan	1,985,642		(35,210)	1,950,432	38,203
Compensated absences	1,211,497		(285,405)	926,092	285,405
Claims and judgments	754,353			754,353	
Property Tax Debt – Law 42	2,249,541		(42,616)	2,206,925	45,293
Property Tax Debt – Law 46	585,358		(24,390)	560,968	24,390
Property Tax Debt – Treasury Department	86,463		(43,232)	43,231	43,231
Landfill obligation	1,505,834	61,909		1,567,743	50,124
LIMS Repayment Plan	104,037		(27,580)	76,457	29,245
Puerto Rico Aqueduct and Sewer Authority	252,000	-	(77,000)	175,000	84,000
Total	\$ 12,707,725	\$ 4,701,909	\$ (803,433)	\$ 16,606,201	\$ 964,891

A. GENERAL OBLIGATIONS BONDS

The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. General obligations bonds as of June 30, 2009, are comprised of the following individual issues:

DESCRIPTION	AMOUNT
\$1,065,000 Series 2000, for operational purposes, payable in annual installments, excluding variable interests from 5% to 8%, through July 1, 2010	\$ 145,000
\$1,410,000 Series 2002, for construction purposes, payable in semiannual installments, excluding variable interests from 2.7% to 5.6%, through July 1, 2026	1,240,000
\$940,000, Series 2002, for operational purposes, payable in semiannual installments, excluding variable interests from 2.2% to 7.5%, through July 1, 2026	830,000
\$1,250,000, Series 2007, for construction purposes, payable in semiannual installments, excluding variable interests from 2.43% to 7.0%, through July 1, 2031	1,210,000
Total General Obligations – Bonds	\$ 3,425,000

These bonds are payable from the special ad valorem property tax of 2.00% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2009**

NOTE 9 – GENERAL LONG-TERM DEBTS (CONTINUED)

A. GENERAL OBLIGATIONS BONDS (CONTINUED)

The annual requirements to amortize these bonds obligations, outstanding as of June 30, 2009, are as follows:

Year Ending June 30,	Principal payment	Interest payment	Total
2010	\$ 230,000	\$ 214,708	\$ 444,708
2011	85,000	230,812	315,812
2012	90,000	198,555	288,555
2013	100,000	192,788	292,788
2014	105,000	186,500	291,500
2015-2019	655,000	820,046	1,475,046
2020-2024	950,000	568,658	1,518,658
2025-2029	925,000	221,083	1,146,083
2030-2034	<u>285,000</u>	<u>30,625</u>	<u>315,625</u>
Total	<u>\$ 3,425,000</u>	<u>\$ 2,663,775</u>	<u>\$ 6,061,775</u>

B. NOTES PAYABLES

The proceeds of the issuance of notes payables are used principally to pay debt incurred in prior years and to cover the expenditures of a special event. Notes payables as of June 30, 2009, are comprised of the following individual issues:

DESCRIPTION	AMOUNT
\$460,000, Series 2004, for construction purposes, payable in annual installments, excluding interests at 4.50%, through July 1, 2013	\$ 280,000
\$4,640,000, Series 2009, for construction purposes, payable in semiannual installments, excluding variable interests from 2.43% to 7.5%, through July 1, 2033	<u>4,640,000</u>
Total Notes Payable	<u>\$ 4,920,000</u>

The Series 2004 note, amounting \$460,000, is payable with operational resources and the Series 2009, amounting \$4,640,000, is payable with municipal sales and uses taxes resources restricted for debt service. The CRIM retains the payment from the property tax advances of the Municipality.

The annual requirements to amortize these bonds obligations, outstanding as of June 30, 2009, are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 9 – GENERAL LONG-TERM DEBTS (CONTINUED)

B. NOTES PAYABLES

Year Ending June 30,	Principal payment	Interest payment	Total
2010	\$ 135,000	\$ 243,012	\$ 378,012
2011	143,000	349,613	492,613
2012	151,000	340,740	491,740
2013	161,000	331,358	492,358
2014	90,000	321,375	411,375
2015-2019	570,000	1,488,750	2,058,750
2020-2024	820,000	1,231,875	2,051,875
2025-2029	1,170,000	862,500	2,032,500
2030-2034	<u>1,680,000</u>	<u>333,000</u>	<u>2,013,000</u>
Total	<u>\$ 4,920,000</u>	<u>\$ 5,502,223</u>	<u>\$ 10,422,223</u>

C. SECTION 515 DIRECT LOAN

Liabilities of \$1,950,432 reported in the statement of net assets represents the outstanding balance of the Housing Project, Section 515 loan payable. This loan is payable in annual installments, excluding variable interests from 7.0% to 9.0%, through July 1, 2033.

D. COMPENSATED ABSENCES

The government-wide statement of net assets includes \$670,069 of accrued sick leave benefits, and \$256,023 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

E. CLAIMS AND JUDGMENTS

Liabilities of \$754,353 reported in the statement of net assets represent the balance owed for claims and judgments at June 30, 2009, as described in Note 18.

F. PROPERTY TAX DEBT – LAW 42

On January 26, 2000, Act No. 42 was enacted to authorize the CRIM to enter into a financing agreement of up to \$200 million, for a term not exceeding 30 years. The financing agreement allows for the financing of a debt that the municipalities of Puerto Rico have with the CRIM, arising from the final settlements of property tax advances versus actual collections through fiscal year 2000. The amounts that the municipalities will collect from the additional property taxes resulting from the increases in the subsidy from the Commonwealth to the municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238 of August 15, 1999. The outstanding balance of the note payable to the CRIM at June 30, 2009 amounted to \$2,206,925.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 9 – GENERAL LONG-TERM DEBTS (CONTINUED)

G. PROPERTY TAX DEBT – LAW 146

On September 24, 2002, the CRIM, on behalf of the municipalities of Puerto Rico, entered into a financing agreement with GDB pursuant to the provisions of Law No. 146 of October 11, 2001. The purpose of this financing agreement was to extinguish in advance certain bonds payable issued by the Public Finance Corporation, a subsidiary of the GDB, which were originally issued to pay certain property tax receivables owned by the municipalities of Puerto Rico through 1996. The outstanding balance of the note payable to the CRIM at June 30, 2009 amounted to \$560,968.

H. PROPERTY TAX DEBT – TREASURY DEPARTMENT

On December 31, 1992, the Municipality entered into an agreement with the Commonwealth of Puerto Rico – Treasury Department, for the repayment of excess property tax advances. As of June 30, 2009, the related unpaid property tax advances presented in the statement of net assets amounted to approximately \$43,231.

I. LANDFILL OBLIGATION

The \$1,567,743 reported as landfill obligation at June 30, 2009, represents an estimate related to closure and post closure costs, as described in Note 10.

J. LIMS REPAYMENT PLAN

During the fiscal year 2001-2002, the Municipality authorized the CRIM to retain the corresponding portion for the financing project of Land Information Management System – LIMS, contracted by the CRIM. A total of \$248,774 is to be retained in a ten years period at an interest rate of 5.95%, until November 28, 2011. At June 30, 2009, the outstanding debt balance was \$74,457. This amount will be presented in the government wide statement of net assets.

k. PUERTO RICO AQUEDUCT AND SEWER AUTHORITY

During past years, the Municipality entered into a financing agreement with Puerto Rico Aqueduct and Sewer Authority, for the payment of the Municipality's debt for water and sewer services. The balance at June 30, 2009 of this agreement was \$175,000.

NOTE 10 – LANDFILL OBLIGATION

State and federal laws and regulations require the Municipality to place a final cover on its landfill site, when it stopped accepting waste, and perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with Statement No. 18 of the GASB, "Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs", the Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations.

Based on this study, the Municipality has recognized \$1,567,743 as the Municipality's estimated current cost for landfill closure and post-closure costs as of June 30, 2009. The annual estimate of post closure costs has been assessed approximately to be \$15,500 for a period of approximately 30 years. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. The balance of closure and post-closure costs are reported in the government-wide statement of net assets.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 11 – DEBT RETIREMENT

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

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

NOTE 12 – PROPERTY TAXES

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

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

The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the final liquidation noting that the collections exceeded advances by \$95,804. In the governmental funds, the entire receivable has been offset by deferred revenue since the excess was not available to pay liabilities of the current period. In the government-wide financial statements, the entire receivable is recognized as revenue.

On December 31, 1992, the Municipality entered into an agreement with the Commonwealth of Puerto Rico – Treasury Department, for the repayment of excess property tax advances. As of June 30, 2009, the related unpaid property tax advances presented in the statement of net assets amounted to approximately \$43,231.

On January 26, 2000, Public Law No. 42 was enacted which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000. The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238, enacted on August 15, 1999. On October 11, 2001, Public Law No. 146 was enacted to amend Public Law No. 42, to extend the loan amortization period up to 30 years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 12 – PROPERTY TAXES (CONTINUED)

Also, on October 11, 2002, Public Law No. 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law No. 42 enacted on January 26, 2000.

On June 26, 1997, Public Law No. 21 was enacted authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable or equivalent in money.

Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law No. 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities thru a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law.

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

The annual tax rate is 8.83% for real property and 6.83% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 2.00% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

NOTE 13 – MUNICIPAL LICENSE TAX

The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives 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 on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2009, the tax rates were as follows:

- ❖ Financial business- 1.50% of gross revenues
- ❖ Other organizations- 0.50% of gross revenues

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 13 – MUNICIPAL LICENSE TAX (CONTINUED)

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2009 net of allowance for uncollectible.

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

NOTE 14 – MUNICIPAL SALES AND USE TAXES

On July 29, 2007, an amended to Act No. 117 of July 4, 2006, known as the "Tax Fairness Act of 2006", was enacted with the purpose of establishing a mandatory sales and use tax of 1.5% at the Municipal Level. The Municipalities of Puerto Rico are responsible to collect 1% of the corresponding tax with the same exemptions and limitations that the portion collected by the Treasury Department. The Act provides an optional surtax on the un-process food. This surtax must be approved by the Municipal Legislature.

The Treasury Department is responsible to create the Municipal Development Fund (.02%), the Municipal Redemption Fund (.02%) and the Municipal Improvements Fund (.01%) with the remaining 0.5%.

On September 2, 2008, the Municipal Legislature approved the transfer of 50% from the Municipal Development Fund to the Municipal Redemption Fund, as approved by Law 64 from July 3, 1996, as amended, to increase its debt issuance capacity. Loans issued with those funds can be used for waste management and recycling activities, construction of infrastructure, health and public safety projects and the payroll expenses related to those programs.

NOTE 15 – INTERGOVERNMENTAL REVENUES

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

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

NOTE 16 – INTERFUND TRANSFERS

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

Transfer Out	Transfer In	Purpose	Amount
General Fund	Debt Service Fund	Debt retirement	\$ 78,435
General Fund	Special Revenue Fund – State and Local Grants	To cover special fund expenditures	50,806
Other Governmental Funds	Debt Service Fund	Debt retirement	178,721
Total			<u>\$ 307,962</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 17 – PENSION PLAN

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

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

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

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

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

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$ 550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions during the year ended June 30, 2009 amounted to \$226,393. This amount represented 100% of the required contribution.

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

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 18 – COMMITMENTS AND CONTINGENCIES

A. CLAIMS AND JUDGMENTS

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

With respect to pending and threatened litigation, the Municipality has reported liabilities of approximately \$754,353 for awarded and anticipated unfavorable judgments. This amount was included in the financial statements and represents the amount estimated as probable liability or a liability with a fixed or expected due date, which will require future available financial resources for its payment.

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

NOTE 19 – ACCOUNTING CHANGES AND RESTATEMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

The following restatements have been made in the governmental fund financial statements, which are reported as an adjustment to the beginning fund balances:

Description	General Fund	Special Revenue Fund – State & Local Grants	Special Revenue Fund Federal Grants	Capital Projects Fund – State & Local Grants	Debt Service Fund	Other Governmental Fund	Total
Fund balance, beginning	\$ (3,503,135)	\$ 2,647,628	\$ 4,562	\$ 1,258,386	\$ 942,047	\$ 760,557	\$ 2,110,045
To correct prior year due to other agency	100,942						100,942
To correct prior year accounts payable				162,716			162,716
To correct prior year adjusted cash balance						51,423	51,423
To reclassify prior year deferred revenues			(4,562)				(4,562)
To eliminate prior year accounts receivable		(54,712)					54,712
To eliminate prior year due from other fund	(75,270)	75,270	-	-	-	-	-
Fund balance, beginning as restated	<u>\$ (3,477,463)</u>	<u>\$ 2,668,186</u>	<u>\$ -</u>	<u>\$ 1,421,102</u>	<u>\$ 942,047</u>	<u>\$ 811,980</u>	<u>\$ 2,365,852</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 19 – ACCOUNTING CHANGES AND RESTATEMENTS (CONTINUED)

B. GOVERNMENTAL WIDE FINANCIAL STATEMENTS

The following restatements have been made in the governmental wide financial statements, which are reported as an adjustment to the beginning net assets:

<u>Description</u>	<u>Total</u>
Net assets, beginning	\$ 16,121,128
To correct prior year due to other agency	100,942
To correct prior year accounts payable	162,716
To correct prior year adjusted cash balance	51,423
To reclassify prior year deferred revenues	(4,562)
To eliminate prior year accounts receivable	<u>(54,712)</u>
Total	<u>\$ 16,376,935</u>

NOTE 20 – SUBSEQUENT EVENTS

A. THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009

The American Recovery and Reinvestment Act of 2009 (ARRA), is an economic stimulus package endorsed by the President of the United States of America, and approved by Congress. This Act is designed primarily to combat the rising unemployment trends, put more money in the hands of consumers, and reduce the likelihood that state and local governments will need to raise taxes significantly. According to the White House press release, the legislation will do the following:

- ❖ Create or save 3.5 million jobs in the next 2 years;
- ❖ Provide direct tax relief to working and middle class families;
- ❖ Double the U.S. renewable energy generating capacity over 3 years;
- ❖ Stimulate private investment in renewable energy through tax credits and loan guarantees;
- ❖ Invest \$150 billion in U.S. infrastructure projects, and;
- ❖ Provide funds to U.S. state and local governments to support health and education programs.

Puerto Rico is part of the American territories that will benefit from the stimulus package of ARRA, and will receive approximately \$5.6 million in grants and is eligible to obtain additional funding through other competitive federal programs. Therefore, the Municipality will benefit from federal grants to improve its services to its constituents and from the economic activity generated within its territory due to projects funded by ARRA.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

NOTE 20 – SUBSEQUENT EVENTS (CONTINUED)

B. INVESTMENT ON OUR INFRASTRUCTURE PLAN (PINI)

On March 9, 2009, the Legislature of the Commonwealth of Puerto Rico approved Law No. 9, which makes feasible the Investment on Our Infrastructure Plan (PINI) to benefit the municipalities of Puerto Rico. The following are the objectives of this Plan:

- ❖ Provide an immediate stimulus to the economy through funding of infrastructure Projects Island wide, and;
- ❖ Speed-up priority infrastructure projects in all municipalities of Puerto Rico.

In the first phase, the municipalities can use the funds for the following:

- ❖ Funding of essential infrastructure, and;
- ❖ Those municipalities with deficit can use those them to partially or fully liquidate existing debts with governmental agencies.

The Municipality assigned these funds for debts to agencies. Those debts were paid between July and August 2009.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

**BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)**

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u> (Budgetary Basis)	<u>Variance with</u> <u>Final Budget</u>
	<u>Original</u>	<u>Final</u>	<u>(See Note 1)</u>	<u>Positive</u> <u>(Negative)</u>
REVENUES:				
Property taxes	\$ 1,365,857	\$ 1,365,857	\$ 1,365,857	\$ -
Fines and forfeiture	2,000	2,000	8,975	6,975
Municipal license tax	712,500	712,500	745,391	32,891
Municipal sales and use tax	415,000	415,000	615,922	200,922
Licenses, permits and other local taxes	450,200	450,200	219,820	(230,380)
Intergovernmental	5,083,219	5,083,219	5,069,847	(13,372)
Rent of property	95,000	95,000	97,257	2,257
Interests	10,000	10,000	138,366	128,366
Miscellaneous	63,500	63,500	672,079	608,579
Total revenues	<u>8,197,276</u>	<u>8,197,276</u>	<u>8,933,514</u>	<u>736,238</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
General government	4,501,203	4,502,222	4,312,647	189,575
Public safety	419,231	362,431	327,481	34,950
Public works	2,215,916	2,267,747	2,436,707	(168,960)
Health and welfare	585,686	585,686	600,904	(15,218)
Culture and recreation	396,805	400,755	387,010	13,745
Operating transfer to other funds	78,435	78,435	78,435	-
Total expenditures, encumbrances and other financing uses	<u>8,197,276</u>	<u>8,197,276</u>	<u>8,143,184</u>	<u>54,092</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 790,330</u>	<u>\$ 790,330</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 8,933,514
Differences-budget to GAAP:				
GAAP adjustments to revenues				<u>85,595</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 9,019,109</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 8,143,184
Differences-budget to GAAP:				
Prior year encumbrances recorded as current year expenditures for GAAP basis				184,538
Current year encumbrances recorded as expenditures for budgetary purposes				(157,680)
GAAP adjustments to expenditures				(78,776)
Non budgetary transfer out				<u>50,806</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 8,142,072</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND

YEAR ENDED JUNE 30, 2009

NOTE 1 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. BUDGETARY CONTROL

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

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

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

The unencumbered balance of any appropriation at the end of the fiscal year will lapse at the end of such fiscal year. Other appropriations, mainly capital project appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2009

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF AGRICULTURE:			
Pass-through the Commonwealth of Puerto Rico Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	\$ 15,477
Total U.S. Department of Agriculture			15,477
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Lower income Housing Assistance Program Section 8 Moderate Rehabilitation	14.856		595,128
Direct Program:			
Section 8 Housing Choice Voucher Program	14.871		452,408
Pass-through the Commonwealth of Puerto Rico – Office of the Commissioner of Municipal Affairs:			
Community Development Block Grants – State's Program	14.228	00-FD-07 01-FD-07 02-AB-FC-RI-07 03-AB-FC-07 04-AB-FC-07 05-AB-FC-07 06-AB-FC-07 07-AB-FC-07	818,168
Total U.S. Department of Housing and Urban Development			1,865,704

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2009

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico Administration for Children and Families (ACUDEN):			
Child Care and Development Block Grant	93.575	Not Available	<u>279,499</u>
Total U.S. Department of Health and Human Services			<u>279,499</u>
U.S. DEPARTMENT OF HOMELAND SECURITY:			
Pass-through the Commonwealth of Puerto Rico - Governor Authorized Representative (GAR):			
Disaster Grants – Public Assistance	97.036	Not Available	307,741
Pass-through the Commonwealth of Puerto Rico Emergency Management Agency:			
Pre-Disaster Mitigation Competitive Grants	97.017	Not Available	15,729
Homeland Security Grant Program	97.067	Not Available	<u>120,800</u>
Total U.S. Department of Homeland Security			<u>444,270</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 2,604,950</u>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2009

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the **Municipality of Arroyo** and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the fund financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

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

Description	Special Revenue Fund – Federal Grants	Other Governmental Funds	Total
Per Schedule of Expenditures of Federal Awards	\$ 1,557,414	\$ 1,047,536	\$ 2,604,950
Non federal programs expenditures	<u>102,580</u>	<u>381,083</u>	<u>483,663</u>
Total expenditures in the general purpose financial statements	<u>\$ 1,659,994</u>	<u>\$ 1,428,619</u>	<u>\$ 3,088,613</u>



López-Vega, CPA, PSC

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

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Arroyo**, Puerto Rico, as of and for the year ended June 30, 2009, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated November 20, 2009, which was unqualified at the governmental-wide financial statement level, but qualified at the fund financial statements level because we were unable to obtain sufficient evidence to support and to satisfy ourselves about the amount recorded in each major fund and the aggregate remaining fund information as due from/ due to other funds and transfer in / transfer out. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

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

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

We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting. (Items 09-01 through 09-02)

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items **09-01** and **09-02** to be material weaknesses.

Compliance and Other Matters

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

We also noted certain other matters that we reported to management of the **Municipality of Arroyo** in a separate letter dated November 20, 2009.

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

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


LOPEZ-VEGA, CPA, PSC

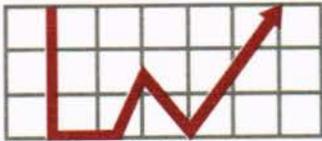
San Juan, Puerto Rico
November 20, 2009

Stamp No. 2407054 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



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

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

Compliance

We have audited the compliance of the **Municipality of Arroyo** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. The **Municipality of Arroyo's** major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the **Municipality of Arroyo's** management. Our responsibility is to express an opinion on the **Municipality of Arroyo's** compliance based on our audit.

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

In our opinion, the **Municipality of Arroyo** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items **09-03** through **09-08**.

Internal Control Over Compliance

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

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

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

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items **09-03** through **09-08** to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider items **09-03**, **09-04**, **09-05** and **09-08** to be material weaknesses.

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

We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Arroyo** in a separate letter dated March 12, 2010.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
March 12, 2010

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2009**

Section I – Summary of Auditor’s Results

Financial Statements

Type of auditor’s report issued:	Unqualified	
Internal control over financial reporting:		
Material weakness identified?	Yes X	No
Significant deficiencies identified not considered to be material weaknesses?	Yes X	None reported
Noncompliance material to financial statements noted?	Yes	No X

Federal awards

Internal Control over major programs:		
Material weakness identified?	Yes X	No
Significant deficiencies identified not considered to be material weaknesses?	Yes X	None reported
Type of auditor’s report issued on compliance for major programs:	Unqualified	
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes X	No

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
14.856	Lower Income Housing Assistance Program Section 8 Moderate Rehabilitation
14.871	Section 8 Housing Choice Voucher Program
14.228	Community Development Block Grants – State’s Program

Dollar threshold used to distinguish between Type A and Type B programs	\$300,000
Auditee qualified as low-risk auditee?	Yes No X

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference	09-01
Requirement	Financial Reporting – Accounting Records
Statement of Condition	During our examination of the Municipality's accounting system, we noted that it does not summarize the transactions in a formal General Ledger, in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal funds). Also, the Municipality's accounting system did not provide to produce its Governmental Wide Financial Statements.
Criteria	Chapter VIII, Article 8.010 of the State Act Number 81 of August 30, 1991 states that the Municipality should maintain an effective and updated accounting system.
Cause of Condition	The Municipality did not establish effective internal control over the transactions recorded on its accounting records. Also, the accounting data is not summarized in the form of a double-entry general ledger record.
Effect of Condition	The Municipality's accounting system did not provide update and complete financial information that present the financial position and the result of operations and the change in fund balances. Such information is necessary to take management decisions.
Recommendation	We recommend that the Municipality should implement internal control and procedures in order to maintain an accounting system that contains information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, interfund transactions, etc.
Questioned Costs	None
Management Response and Corrective Action	The Municipality maintains two set of accounting records; a manual system and a computerized system provided in the past by the Office of the Commissioner of Municipal Affairs (OCAM). Actually, all of the transactions were recorded in both systems, but the manual system is the primary financial records for financial statements preparation purposes at the end of each fiscal year due to the fact that the computerized system real accounts balances carried forward from prior years were affected by accounting errors in the first years of the system operation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference 09-01 (Continued)

Management Response
and Corrective Action
(Continued)

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

Implementation Date: Not available at moment

Responsible Person: Mr. Néstor Alicea
Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference 09-02

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

Statement of Condition We performed a cash disbursements test and examined seventeen (17) payments which belonged to General Fund, three (3) which belonged to Law Number 43 account, five (5) which belonged to Permanent Improvements account, two (2) which belonged to Municipality Improvements account, twenty one (21) which belonged to Community Facilities Loans and Grants (AFI) and thirteen (13) which belonged to Community Development Block Grants – State’s Program (CDBG). The following will summarize the internal control exceptions noted:

- a. In four (4) payment which belonged to General Fund, three (3) which belonged to Joint Resolutions and one (1) which belonged to Community Development Block Grants – State’s Program, two (2) which belonged to Permanent Improvements account, one (1) which belonged to Municipality Improvements account, five (5) which belonged to Community Facilities Loans and Grants (AFI), thirteen (13) disbursement vouchers did not include the date and the signature of the Pre-Intervention Officer;
- b. The Municipality did not provide for our examination seven (7) disbursement vouchers and its supporting documents (two (2) related to Community Facilities Loans and Grants (AFI) and five (5) related to General Fund.)

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

Cause of Condition The Municipality internal control procedures failed to assure that all transactions include all the required documentation and approvals.

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

Recommendation We recommend that the Municipality should improve its internal control and procedures in order to assure that the disbursement vouchers contain all the necessary supporting documents before making the payments and are available for examination.

Questioned Costs None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section II – Financial Statements Findings

Finding Reference 09-02 (Continued)

**Management Response
and Corrective Action**

Management will instruct the Finance Department staff (including the Official Payer, the Pre-interventor, the Department Accountant, the Department Secretary, etc.) to strengthen the procedures established in the regulation, in order to assure that the disbursement vouchers contain all the necessary supporting documents and approvals before making the payments. Also, the Municipality instruct its personnel to assure that proper filing of documents are performed so that disbursement vouchers and their justificants are available for examination at any time.

Implementation Date: January, 2011

Responsible Person: Mr. Néstor Alicea
Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	09-03
Programs	Section 8 Lower Income Housing Assistance Program-Section 8 Moderate Rehabilitation (CFDA 14.856) U.S. Department of Housing and Urban Development Section 8 Housing Choice Vouchers Program (CFDA 14.871); U.S. Department of Housing and Urban Development
Requirement	Special Test – Selection from the Section 8 Waiting List
Statement of Condition	In our Waiting List test, we noted the following situation: a) During the year, the Municipal Housing office was robbed. Several documents and programs' equipment were taken from the premises, including computers where the program kept the waiting list. We could not verify the process of admission of new participants in the programs due to this situation.
Criteria	Code of Federal Regulations 24, Sections 982.54 (d) and 982.201 through 982.207 states the waiting list procedures and that the selection from the waiting list generally occurs when the PHA notifies a family, whose names reaches the top of the waiting list, to come in to verify eligibility for admission.
Cause of Condition	The Municipality internal control procedures failed to assure that the waiting list include all information required by Federal Regulation and that the participants were selected from the top of the waiting list.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, sections 982.54 (d) and 982.201 through 982.207.
Recommendation	We recommend management to improve monitoring procedures to assure that the participants are admitted to the program or are provided the opportunity to be admitted to the program according with the federal regulation. Also, we recommend management to establish control procedures to maintain a waiting list with all information required by the Federal Regulation (applicant name, family unit size, date and time of application, qualification for any local preference and ethnic designation of the head of household). This control must permit proper tracing of participants selected in the waiting list in order to assure the selection from the top of the waiting list.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 09-03 (Continued)

Questioned Costs None

**Management Response
and Correction Action**

This situation was due to a break and entry robbery in the program's facilities. We have reinforced the security of the files and the personal information inside the premises and expect that this situation will not occur again. Nevertheless, as part of our corrective action plan, we will document all vouchers issued and its waiting list selection process.

Implementation Date: April, 2010

Responsible Person: Mr. Luis A. Torres Mariani
Section 8 Program Coordinator

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	09-04
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Housing Quality Standards Inspections and HQS Enforcement
Statement of Condition	During our verification, the Municipality did not perform the required Housing Quality Control re-inspections during the fiscal year 2008-2009.
Criteria	Code of Federal Regulations 24, Subpart I, 982.404 and Section 982.158 (d) and 982.405 (b) states that the PHA must inspect the unit leased to a family at least annually to determine if the unit meets Housing Quality Standards (HQS) and the PHA must conduct quality control re-inspections. Also the PHA must prepare a unit inspection report.
Cause of Condition	The Municipality did not maintain adequate monitoring procedures to assure that annual re-inspections Housing Quality Control re-inspections are properly performed.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Section 982.404 and 982.158 (d) and 982.405 (b).
Recommendation	We recommend management to implement internal control procedures to assure that annual inspections and quality control re-inspections are properly performed. The PHA supervisor or other qualified person must re-inspect a sample of units under contract during the last PHA fiscal year. Completed HQS inspections included in the sample must be no older than three months at the time of re-inspection. In addition, the quality control re-inspection should provide feedback on inspector's work, which can be used to determine if individual performance or general HQS training issues need to be addressed.
Questioned Costs	None
Management Response and Corrective Action	The Quality Control Re-inspections will be performed in accordance with our Administrative Plan, revised on March 2010 . Implementation Date: April 1, 2010 Responsible Person: Mr. Luis A. Torres Mariani Federal Programs Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	09-05
Program	Community Development Block Grants – State’s Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico – Office of Commissioner of Municipal Affairs (OCAM)
Requirement	Allowable Activities
Statement of Condition	During our audit, the Municipality did not maintain Housing Rehabilitation records for the fiscal year ended June 30, 2009, to present the position and the results of operations of the Program.
Criteria	<p>Code of Federal Regulations 24, Section 570.506 (b) state that at a minimum, the grantee should maintain records demonstrating that each activity undertaken meets one of the three national objectives of the CDBG Program, i.e., benefit low- and moderate-income persons, prevent or eliminate slums or blight, or meet community development needs having a particular urgency. Also, Code of Federal Regulations 24, Section 570.506 (b) (9) states that when CDBG- State Program funds are used for residential rehabilitation activity to aid in the prevention or elimination of slums or blight in a slum or blighted area, the grantee must maintain records to support the local definition of “substandard”, must document a pre-rehabilitation inspection report describing the deficiencies in each structure to be rehabilitated, and must document the details and scope of CDBG assisted rehabilitation, by structure.</p> <p>In addition, the Municipality has an operational guide that includes all procedures and program’s requirements for housing rehabilitation activities.</p>
Cause of Condition	The Municipality’s controls and procedures failed to assure that all participant’s files, regarding housing rehabilitation activities, were duly documented as required by regulation.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Section 570.506 (b), Section 570.506 (b) (9), and with the operational guide.
Recommendation	We recommend Management to instruct and monitor program staff to created file follow procedures established by the Program, regarding housing rehabilitation activities. This should include completion of all eligibility and inspections forms established in the operational guide.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 09-05 (Continued)

**Management Response
and Corrective Action**

As part of our correction action plan, we gave specific instructions to the program staff to assure that the procedures established by the regulation are followed. Also, the program will monitor its staff for compliance with its regulations.

Implementation Date: April, 2010

Responsible Person: Mr. Jimmy Delucca Guzmán
Federal Program Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	09-06
Program	Community Development Block Grants – State’s Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico – Office of Commissioner of Municipal Affairs (OCAM)
Requirement	Allowable Activities
Statement of Condition	<p>We performed a housekeeper activities test of ten (10) participant’s files and found the following exception:</p> <ul style="list-style-type: none">a) In one (1) participant’s files, we did not find evidence that demonstrate if the program staff visited at least two (2) times per month the participant housing unit to ensure the quality of services.b) In ten (10) participant’s file, we noted that the Service Coordinator did not performed visit to the applicant housing unit to verify location of it.c) In two (2) participant’s files, we noted that, as part of the visits procedures, the Service Coordinator did not document in the Form OCAM-AH-006, the housekeeper performance.
Criteria	Code of Federal Regulations 24, Section 570.484 states that the Municipality must assure that the program funds benefit very low, low- and moderate income persons and retain documentation justifying its certification. Also, the Municipality has an operational guide that includes all procedures and program’s requirements for housekeeper activities.
Cause of Condition	The Municipality’s controls and procedures failed to assure that the program staff follows the procedures includes in the operational guide, in order to comply with the program requirements.
Effect of Condition	The Municipality is not in compliance with the Code of Federal Regulations 24, Section 570.484 and with the operational guide.
Recommendation	We recommended the program staff to follow the procedures established in the procedures manual, including the use of the forms included on it.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference 09-06 (Continued)

**Management Response
and Corrective Action**

We expect to assign a Program staff with the responsibilities to maintain the participants' files in compliance the Program regulations (to follow all the procedures and to use all forms specified in the procedures guide). We are going to discuss the procedures guide "Guía Operacional para la Prestación del Servicio de Auxiliares en el Hogar" with the Program staff and with the municipal employees assigned to the Municipal Elderly Affairs Department and enforce its content with respect to on-site visits.

Implementation Date: April, 2010

Responsible Person: Mr. Jimmy Delucca Guzmán
Federal Program Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	09-07
Program	Community Development Block Grants – State's Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico – Office of Commissioner of Municipal Affairs (OCAM)
Requirement	Cash Management
Statement of Condition	<p>During our Cash Management test, we noted that the Municipality requested funds that were not disbursed on a reasonable lapse of time. We selected a sample of six (6) fund requisitions (a total of \$529,719) and found the following exception:</p> <p>a) In three (3) fund requisitions (a total of \$175,127), we observed that the Municipality made the disbursements between six (6) and thirty six (36) days after the deposits.</p>
Criteria	Code of Federal Regulations 24, Subpart I, Sec.570.489 (c) requires a cash management system in order to minimize the time elapsed between the transfer of funds from the pass-through grantor and disbursements made by the grantee.
Cause of Condition	The Municipality's disbursements procedures failed to assure that funds requested and received from the Pass-through Grantor be disbursed in compliance with the Code of Federal Regulations Requirements.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Sec.570.489 (c).
Recommendation	We recommend management to strengthen its disbursement procedures to minimize the time elapsed between the transfer of funds from the Pass-through Grantor and the disbursements made by the Municipality.
Questioned Costs	None
Management Response and Corrective Action	<p>To correct the condition reported by the external auditors, our Program accountant will plan with the Municipality's Finance Director to start the disbursement process when the requisitions of funds are submitted to the Office of the Commissioner of Municipal Affairs (OCAM) in order to assure that when the funds are transferred by the Pass-through Grantor, we will disburse its immediately.</p>

Implementation Date: April, 2010

Responsible Person: Mr. Jimmy Delucca Guzmán
Federal Program Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2009

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	09-08
Program	Community Development Block Grants – State’s Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico – Office of Commissioner of Municipal Affairs (OCAM)
Requirement	Davis-Bacon Act
Statement of Condition	During our Davis-Bacon Act test of one (1) construction project, we noted that the Municipality did not have evidence to determine if the contractor complied with the dispositions established in the Davis Bacon Act.
Criteria	Davis-Bacon Act, as amended DOL (40 USC 276a to 276a-7).
Cause of Condition	The Municipality’s controls and procedures failed to apply all monitoring system procedures developed to test applicable contractors with respect to payment of prevailing wages.
Effect of Condition	The Municipality is not in compliance with Davis-Bacon Act, as amended DOL (40 USC 276a to 276a-7).
Recommendation	We recommend management to follow monitoring system procedures developed, including create a file to obtaining contractor’s and subcontractor’s weekly payrolls to be reviewed on a weekly basis by the responsible municipal employee, and interview contractor’s and subcontractor’s laborers periodically (up to ten percent (10%) of the workers on long term projects) to establish the degree of compliance and the nature and extend of violations, if any, and then, communicate contractors, promptly, about any failure in the payroll process.
Questioned Costs	None
Management Response and Corrective Action	As part of our corrective action plan, we gave instructions to the program staff to perform the required visits to the project, in order to monitor the classifications of the workers. Also, we gave instructions to program staff to monitor the weekly payrolls provided by the contractor, in order to verify the contractor’s compliance with respect to payment of prevailing wages.
	Implementation Date: April, 2010
	Responsible Person: Mr. Jimmy Delucca Guzmán Federal Program Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2009

Original Finding Number	CFDA No.	Current Status of Prior Audit Findings
08-04	14.856	<p><u>In fifteen (15) participant's files, related to Section 8 Moderate Rehabilitation, we noted the following situation; In two (2) participant's files, we did not observe evidence of the Form HUD-50058, Family Report (OMB No. 2577-0083), applicable for the fiscal year audited.</u></p> <p>Corrective action was taken.</p>
08-04	14.871	<p><u>In fifteen (15) participant's files, related to Section 8 Housing Choice Vouchers, we noted the following situation; In two (2) participant's files, we did not observe evidence of the Form HUD-50058, Family Report (OMB No. 2577-0083), applicable for the fiscal year audited.</u></p> <p>Corrective action was taken.</p>
08-05	14.856	<p><u>In fifteen (15) participant's files, related to Section 8 Moderate Rehabilitation, we noted the following situation: Eight (8) participant's files did not contain evidence demonstrating that the Municipality followed-up the deficiencies noted on the unit inspection.</u></p> <p>Corrective action was taken.</p>
08-05	14.871	<p><u>In fifteen (15) participant's files, related to Section 8 Housing Choice Vouchers, we noted the following situation: One (1) participant's file did not contain evidence demonstrating that the owner corrected an electricity problem identified in the inspection.</u></p> <p>Corrective action was taken</p>
08-06	14.856 & 14.871	<p><u>The waiting list was not prepared according with the federal and local regulation. This list did not include; the dates and the time of application, qualification for any local preference and racial or ethnic designation of the head of household;</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-03.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

Original Finding Number	CFDA No.	Current Status of Prior Audit Findings
08-06	14.856 & 14.871	<p><u>The PHA did not have written policies in its administrative plan for selecting applicants from the waiting list.</u></p> <p>Corrective action was taken</p>
08-06	14.856 & 14.871	<p><u>The auditors performed examined nine (9) files related to new participants admitted in the programs during the fiscal year ended on June 30, 2008 [three (3) related to Section 8 Moderate Rehabilitation and six (6) related to Section 8 Housing Choice Vouchers]. We noted that the PHA did not maintain evidence that demonstrate that these participants were selected from the Waiting List.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-04.</p>
08-07	14.228	<p><u>The auditors performed a housing rehabilitation test of ten (10) participant files and found the following exceptions: In one (1) participant's file, we did not identify documental evidence that confirms the disabilities of the applicant In two (2) participant's files, the rehabilitation contract did not include the deficiencies to be corrected; In one (1) participant's file, the applicant eligibility determination was not completed; In the ten (10) participant's files, we did not observe evidence of the Program Inspector's initial, intermediate and final visits.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-05.</p>
08-08	14.228	<p><u>The auditors performed of housekeeper activities test of eight (8) participant's files and found the following exception: in eight (8) participant's files, we did not find evidence that demonstrate if the program staff visited at least two (2) times per month the participant housing unit to ensure the quality of services.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-06.</p>
08-09	14.228	<p><u>Financial Statements Findings- Finding Reference 08-03.</u></p> <p>Corrective action was taken.</p>

**COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

Original Finding Number	CFDA No.	Current Status of Prior Audit Findings
08-10	14.228	<p><u>During the Davis-Bacon Act test of five (5) construction projects, we noted that the Municipality did not perform procedures in order to determine if the contractors complied with the dispositions established in the Davis Bacon Act; contractor's laborers interviews were not made and contractor's weekly payrolls were not requested during construction period</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-08.</p>
07-05	14.871	<p><u>In the Waiting List Test, the auditors did not obtain evidence that demonstrate if the selection of four (4) participants admitted in the Program during the fiscal year 2006-2007 was in accordance with the waiting list policies established in the administrative plan.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-03.</p>
07-07	14.228	<p><u>The auditors performed a housing rehabilitation test of nine (9) participant files and found the following exceptions: (a) In two (2) participant's files, the auditors did not identify evidence of the pre-rehabilitation inspection; (b) In five (5) participant's files, the auditors did not found evidence that demonstrated if the deficiencies to be corrected were incorporated into a rehabilitation contract; (c) In nine (9) participant's files, the applicant eligibility determination was not documented; (d) In nine (9) participant's files, the auditors did not observed evidence of the program's inspector final visit.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-05.</p>
07-08	14.228	<p><u>During the Davis-Bacon Act test of three (3) construction projects, the auditors noted that the Municipality did not perform the required visits for monitoring the classifications of the workers and the wage rates paid. Also, the weekly payrolls provided by the contractor were not monitored to verify the compliance with the prevailing wage rates.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 09-08.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ARROYO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2009

Original Finding Number	CFDA No.	Current Status of Prior Audit Findings
07-10	93.575	<p><u>During the examination, the auditors noted that the Municipality did not maintain, for the Child Care and Development Block Grant Program, a reliable set of accounting records that present the financial position of the program and the results of its operations.</u></p> <p>No corrective action was taken.</p>
06-04	14.871	<p><u>In the Waiting List test, the auditors noted the following situation: In a sample of twenty five (25) applicants included in the Waiting List, the auditors observed that the PHA did not maintain the required information to assure that the selection of new tenants admitted to the program were in accordance with the administrative plan.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
06-06	14.228	<p><u>The auditors performed a housing rehabilitation test of ten (10) participant files and found the following exceptions: (a) In two (2) participant's files, the auditors did not observe evidence of the program's inspector visits to follow up the rehabilitation work; (b) In eight (8) participant's files, the auditors did not observe evidence of the program's inspector final visit. Also, six (6) of these files did not include photos of the completion of the rehabilitation works; (c) In one (1) participant's file, the auditors observed evidence of the program's inspector final visit; however, it did not include photos of the completion of the rehabilitation works.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
06-10	14.228	<p><u>During the Davis-Bacon Act test of two (2) construction projects, the auditors noted that the Municipality did not perform the required visits for monitoring the classifications of the workers and the wage rates paid. Also, the weekly payrolls provided by the contractor were not monitored to verify the compliance with the prevailing wage rates (for one (1) project, the contractor did not submit all the required certified payrolls).</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>