

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES

AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE CAGUAS

AUDITORIA 2005-2006

30 DE JUNIO DE 2006

OFICINA DEL COMISIONADO
DE ASUNTOS MUNICIPALES

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS**

**FINANCIAL STATEMENTS
(with Independent Auditors' Report Thereon)**

**FISCAL YEAR ENDED
JUNE 30, 2006**

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TABLE OF CONTENTS

	<u>Page</u>
Independent Auditors' Report	1-2
Management's Discussion and Analysis	3-15
Government Wide Financial Statements:	
Statement of Net Assets	16-17
Statement of Activities	18
Fund Financial Statements:	
Governmental Fund Balance Sheet	19-20
Reconciliation of Fund Balance of Governmental Funds to Net Assets of Governmental Activities	21
Statement of Revenues, Expenditures and Changes in Fund Balances	22-23
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statements of Activities	24
Statement of Revenues, Expenditures-Budget and Actual-General Fund	25
Statement of Net Assets-Proprietary Funds	26-27
Statement of Revenues, Expenses and Changes in Net Assets- Proprietary Funds	28
Statement of Cash Flows-Proprietary Funds	29
Notes to Financial Statements	30-63

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INDEPENDENT AUDITORS' REPORT

Hon. William Miranda Marín
Major
Municipality of Caguas, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Municipality of Caguas, Puerto Rico, as of and for the fiscal year ended June 30, 2006, 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 an opinion 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; the standards applicable to financial audits contained in the Government Auditing Standards, issued by the Comptroller General of the United States of America; and OMB Circular A-133, Audits of States, Local Governments, and Non Profit Organizations. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Municipality of Caguas, Puerto Rico, as of June 30, 2006, and the respective changes in financial position and, where applicable, cash flows thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

Telephone: (787) 754-6615 - Telefax: (787) 765-9405
Email: pkfpr@pkfpr.com
PKF, LLP
1056 Muñoz Rivera Avenue, Suite 304
San Juan, PR 00927-5013

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Accountants &
business advisers

Hon. William Miranda Marín
Major
Municipality of Caguas

In accordance with Government Auditing Standards, we have also issued our report dated December 15, 2006 on our consideration of the Municipality of Caguas'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 15 and budgetary comparison information on page 25 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.



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License No. 22
Expires December 1, 2007

December 15, 2006



To the Citizens and the Municipal Legislature
of the City of Caguas

Management's Discussion and Analysis

As management of the Autonomous Municipality of Caguas (hereafter the Municipality), we offer readers of the Municipality's financial statements this narrative overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2006. We encourage readers to read the information presented here in conjunction with the accompanying Transmittal Letter and the basic financial statements.

Financial Highlights

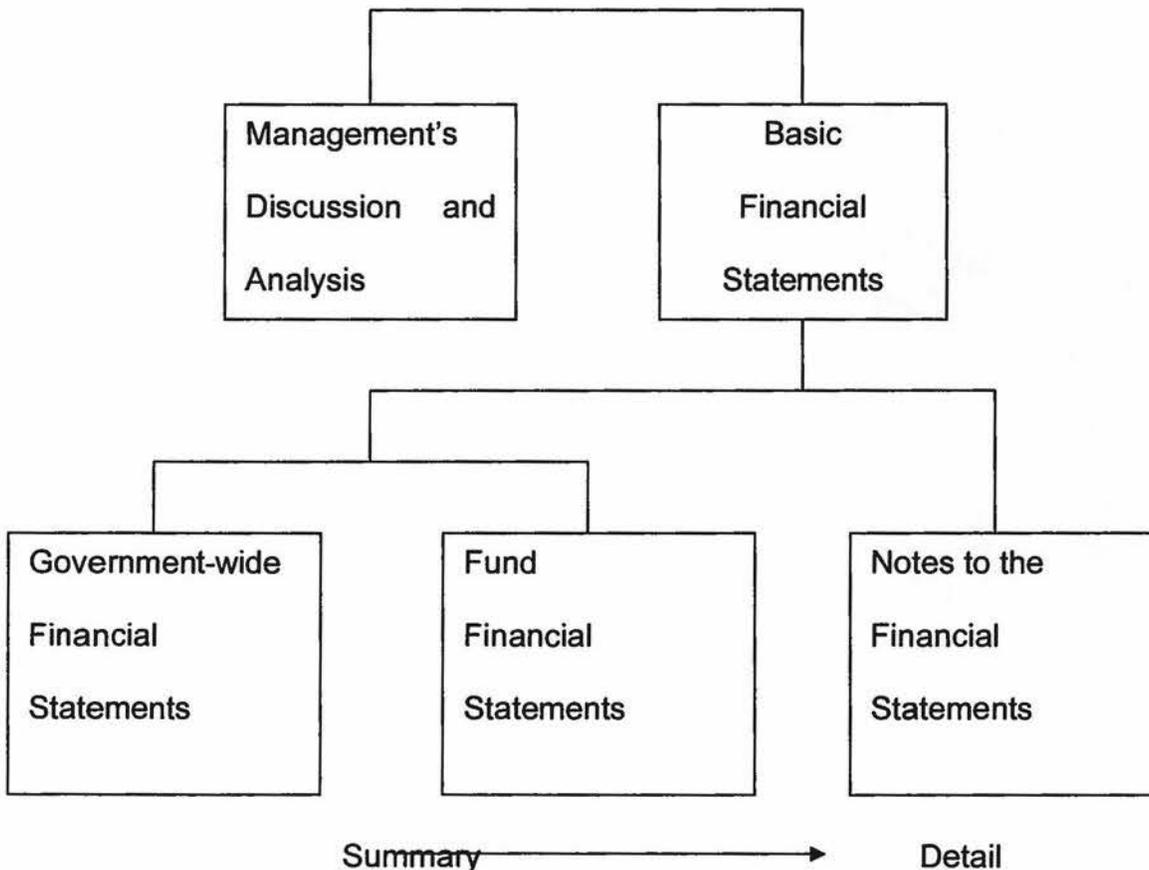
- The assets of the Municipality exceeded its liabilities at the close of the fiscal year by \$256,270,113 (*net assets*).
- The government's total net assets increased by \$15,961,652, primarily due to increased in Governmental Activities revenues.
- As of the close of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$84,832,010, after a net increase in fund balance of \$35,982,230. Approximately 41.40 percent of this total amount, or \$14,913,915, is available for spending at the government's discretion (*unreserved fund balance*).
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$14,913,915, or 16.4 percent of total general fund expenditures for the fiscal year.
- The Municipality's total debt increased by \$36,515,565 (30%) during the current fiscal year. The key factors in this increase are the \$24.175 million in bonds issued for infrastructure development and \$20.090 million of special loans used for infrastructure development.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the Municipality's basic financial statements. The Municipality's basic financial statements consist of three components; 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements (see Figure 1). The basic financial statements present two different views of the Municipality through the use of government-wide statements and fund financial statements. In addition to the basic financial statements, this report contains other supplemental information that will enhance the reader's understanding of the financial condition of the Municipality.

Required Components of Annual Financial Report

Figure 1



Basic Financial Statements

The first two statements (Pages 16 through 18) in the basic financial statements are the **Government-wide Financial Statements**. They provide both short and long-term information about the Municipality's financial status.

The next statements (Pages 19 through 29) are **Fund Financial Statements**. These statements focus on the activities of the individual parts of the Municipality's government. These statements provide more detail than the government-wide statements. There are four parts to the Fund Financial Statements: 1) the governmental funds statements; 2) the budgetary comparison statements; and 3) the proprietary fund statements.

The next section of the basic financial statements is the **notes**. The notes to the financial statements explain in detail some of the data contained in those statements.

Government-wide Financial Statements

The government-wide financial statements are designed to provide the reader with a broad overview of the Municipality's finances, similar in format to a financial statement of a private-sector business. The government-wide statements provide short and long-term information about the Municipality's financial status as a whole.

The two government-wide statements report the Municipality's net assets and how they have changed. Net assets are the difference between the Municipality's total assets and total liabilities. Measuring net assets is one way to evaluate the Municipality's financial condition.

The government-wide statements are divided into two categories: 1) governmental activities; and 2) business-type activities. The governmental activities include most of the Municipality's basic services such as public safety, parks and recreation, and general administration. Property taxes and state and federal grant funds finance most of these activities. The business-type activities are those that the Municipality charges customers to provide. These include Community Development Bank and multi-tenant activities.

The government-wide financial statements are from Pages 16 through 18 of this report.

Fund Financial Statements

The fund financial statements provide a more detailed look at the Municipality's most significant activities. 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 all other governmental entities in the Commonwealth of Puerto Rico, uses fund accounting to ensure and reflect compliance (or non-compliance) with finance-related legal requirements, such as the General Statutes or the Municipality's budget ordinance. All of the funds of the Municipality can be divided into two categories: governmental funds and proprietary funds.

Governmental Funds – Governmental funds are used to account for those functions reported as governmental activities in the government-wide financial statements. Most of the Municipality's basic services are accounted for in governmental funds. These funds focus on how assets can readily be converted into cash flow in and out, and what monies are left at year-end that will be available for spending in the next year. Governmental funds are reported using an accounting method called *modified accrual accounting*. This method also has a current financial resources focus. As a result, the governmental fund financial statements give the reader a detailed short-term view that helps him or her determine if there are more or less financial resources available to finance the Municipality's programs. The relationship between government activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is described in a reconciliations that are a part of the fund financial statements (see pages 21 and 24).

The Municipality adopts an annual budget for its General Fund, as required by the General Statutes. The budget is a legally adopted document that incorporates input from the citizens of the Municipality, the management of the Municipality, and the decisions of the Board about which services to provide and how to pay for them. It also authorizes the Municipality to obtain funds from identified sources to finance these current period activities. The budgetary statement provided for the General Fund demonstrates how well the Municipality complied with the budget ordinance and whether or not the Municipality succeeded in providing the services as planned when the budget was adopted. The budgetary comparison statement uses the budgetary basis of accounting and is presented using the same format, language, and classifications as the legal budget document. The statement shows four columns: 1) the original budget as adopted by the board; 2) the final budget as amended by the board; 3) the actual resources, charges to appropriations, and ending balances in the General Fund; and 4) the difference or variance between the final budget and the actual resources and charges (see page 25).

Proprietary Funds – The Municipality has one kind of proprietary fund. *Enterprise Funds* are used to report the same functions presented as business-type activities in the government-wide financial statements. The Municipality uses enterprise funds to account for its Government Development Bank activity and for its multi-tenant operations. These funds are the same as those separate activities shown in the business-type activities in the Statement of Net Assets and the Statement of Activities (see Pages 26 through 29).

Notes to the 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. The notes to the financial statements start on pages 30 through 63 of this report.

Government-Wide Financial Analysis

As noted earlier, net assets may serve over time as one useful indicator of a government's financial condition. The assets of the Municipality exceeded liabilities by \$256,270,113 as of June 30, 2006. The Municipality's net assets increased by \$15,961,652 for the fiscal year ended June 30, 2006. One of the largest portions (75%) reflects the Municipality's investment in capital assets (e.g. land, buildings, infrastructure, and equipment), less any related debt still outstanding that was issued to acquire those items. The Municipality uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the Municipality's investment in its capital assets is reported net of the outstanding related debt, the resources needed to repay that debt must be provided by other sources, since the capital assets cannot be used to liquidate these liabilities. An additional portion of the Municipality's net assets (21%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of \$8,784,158 is unrestricted.

The Municipality's Net Assets

Figure 2

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Current and other assets	\$ 132,743,458	\$ 95,268,346	\$ 4,148,947	\$ 3,538,346	\$ 136,892,405	\$ 98,806,692
Capital assets	326,229,982	303,694,001	7,475,356	5,046,889	333,705,338	308,740,890
Loan receivable, net	-	-	1,562,614	2,657,515	1,562,614	2,657,515
Total assets	<u>458,973,440</u>	<u>398,962,347</u>	<u>13,186,917</u>	<u>11,242,750</u>	<u>472,160,357</u>	<u>410,205,097</u>
Current liabilities	57,405,839	49,321,101	490,223	668,916	57,896,062	49,990,017
Other liabilities	157,600,631	120,872,802	393,551	493,105	157,994,182	121,365,907
Total liabilities	<u>215,006,470</u>	<u>170,193,903</u>	<u>883,774</u>	<u>1,162,021</u>	<u>215,890,244</u>	<u>171,355,924</u>
Net assets:						
Invested in capital assets, net of related debt	184,676,300	190,035,452	7,813,633	5,057,186	192,489,933	195,092,638
Restricted	52,943,537	33,633,180	2,052,485	2,657,515	54,996,022	36,290,695
Unrestricted	6,347,133	5,099,812	2,437,025	2,366,028	8,784,158	7,465,840
Total net assets	<u>\$ 243,966,970</u>	<u>\$ 228,768,444</u>	<u>\$ 12,303,143</u>	<u>\$ 10,080,729</u>	<u>\$ 256,270,113</u>	<u>\$ 238,849,173</u>

Several particular aspects of the Municipality's financial operations positively influenced the total unrestricted governmental net assets:

- Continued diligence in the collection of property taxes by maintaining a collection percentage of 98%.
- Increased charges for services revenue due to growth in the use of Municipality facilities.
- Continued low cost of debt due to the Municipality's high bond rating.

The Municipality's Changes in Net Assets

Figure 3

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2,006	2005	2006	2005
Revenues:						
Program revenues:						
Charges for services	\$ 5,656,459	\$ 1,801,546	\$ 345,031	\$ 375,932	\$ 6,001,490	\$ 2,177,478
Operating grants and contributions	43,037,022	32,187,682	-	-	43,037,022	32,187,682
Capital grants and contributions	6,164,373	12,030,475	653,223	-	6,817,596	12,030,475
Other	-	-	-	3,313,868	-	3,313,868
General revenues:						
Property taxes	52,535,437	43,617,542	-	-	52,535,437	43,617,542
Other taxes	36,808,387	20,605,115	-	-	36,808,387	20,605,115
Licenses and permits	9,374,513	7,617,979	-	-	9,374,513	7,617,979
Interest and investment income	2,369,454	882,881	37,035	18,402	2,406,489	901,283
Total revenues	155,945,645	118,743,220	1,035,289	3,708,202	156,980,934	122,451,422
Expenses:						
General government	38,310,363	36,777,337	-	-	38,310,363	36,777,337
Public safety	8,797,955	7,910,265	-	-	8,797,955	7,910,265
Public works	24,469,027	25,612,960	-	-	24,469,027	25,612,960
Cultural and recreation	8,276,237	9,141,506	-	-	8,276,237	9,141,506
Human and wealthwre	9,295,701	8,596,779	-	-	9,295,701	8,596,779
Economic development	4,133,619	3,631,792	-	-	4,133,619	3,631,792
Sanitation and environmental	12,633,171	11,903,917	-	-	12,633,171	11,903,917
Housing	11,737,150	10,033,232	-	-	11,737,150	10,033,232
Education	15,234,980	12,912,375	-	-	15,234,980	12,912,375
Debt service	7,767,626	5,474,057	-	-	7,767,626	5,474,057
Community Development Bank	-	-	234,539	549,047	234,539	549,047
Multitenant	-	-	128,914	112,232	128,914	112,232
Total expenses	140,655,829	131,994,220	363,453	661,279	141,019,282	132,655,499
Increase (decrease) In net assets before transfer	15,289,816	(13,251,000)	671,836	3,046,923	15,961,652	(10,204,077)
Transfer	-	5,073,092	-	(5,073,092)	-	-
Net increase (decrease) in net assets	15,289,816	(8,177,908)	671,836	(2,026,169)	15,961,652	(10,204,077)
Net assets, beginning as previously reported	150,019,996	150,019,996	10,080,729	13,657,476	160,100,725	163,677,472
Prior period adjustments	78,657,158	86,926,356	1,550,578	(1,550,578)	80,207,736	85,375,778
Net assets, beginning as restated	228,677,154	236,946,352	11,631,307	12,106,898	240,308,461	249,053,250
Net assets, ending	\$ 243,966,970	\$ 228,768,444	\$ 12,303,143	\$ 10,080,729	\$ 256,270,113	\$ 238,849,173

Governmental activities. Governmental activities increased the Municipality's net assets by \$15,289,816, thereby accounting for 95.80% of the total growth in the net assets of the Municipality. Key elements of this increase are as follows:

- Total revenues increased 31% over prior year reported.
 - Increase in other taxes (including the newly adopted city tax)
 - Increase in property tax due primarily to an increase in the tax rate portion of the debt redemption fund and a high tax collection rate.
 - Increase in interest and investment income for savings and other investments
 - Increasing license and permits for new development and construction projects
- Total expenses increased by 6%

Business-type activities: Business-type activities increased the Municipality's net assets by \$671,836, accounting for 4.2% of the total growth in the government's net assets. Key elements of this increase are as follows:

- Activities related to Parque del Turabo were closed under the provisions of the GASB 42 (Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries). This cause an economy in the business type activities of approximately \$148,000
- Costs related to the Fine Art Center were transferred to the Capital Project Fund as of June 30, 2005 (see Note 9 of the financial statements)

Financial Analysis of the Municipality's Funds

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

Governmental Funds. The focus of The Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of usable resources. Such information is useful in assessing the Municipality's financing requirements. Specifically, unreserved fund balance can be a useful measure of a government's net resources available for spending at the end of the fiscal year.

The General Fund is the main operating fund of the Municipality. At the end of the current fiscal year, unreserved fund balance of the General Fund was \$14,913,915, while total fund balance reached \$31,207,829. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 16.4 percent of total General Fund expenditures, while total fund balance represents 34.3 percent of that same amount.

At June 30, 2006, the governmental funds of the Municipality reported a combined fund balance of \$84,832,010, a 70.67 percent increase over last year. The primary reason for this increase is the increase in fund balance in the General Fund, Housing Rental, Capital Projects Fund and Debt Service Fund.

General Fund Budgetary Highlights: During the fiscal year, the Municipality revised the budget on several occasions. Generally, budget amendments fall into one of three categories: 1) amendments made to adjust the estimates that are used to prepare the original budget ordinance once exact information is available; 2) amendments made to recognize new funding amounts from external sources, such as Federal and State grants; and 3) increases in appropriations that become necessary to maintain services. Total amendments to the General Fund increase revenues by \$31,078,997.

**THE MUNICIPALITY'S BUDGET ACTIVITY
FIGURE 4**

	Original	Orders	Transfers	Final
Resources:				
Property taxes	\$ 34,648,877	-	-	34,648,877
Volume of business taxes	24,250,000	-	-	24,250,000
Sales taxes	-	-	7,515,140	7,515,140
Licenses and permits	9,228,000	-	-	9,228,000
Fines and penalties	1,000,000	-	-	1,000,000
Interest and investment income	1,000,000	-	-	1,000,000
Intergovernmental	8,325,071	-	-	8,325,071
Parking lot fees	174,919	-	-	174,919
Rent	339,821	-	-	339,821
Other resources	89,300	14,180,371	9,383,486	23,653,157
Amounts available for appropriation	<u>79,055,988</u>	<u>14,180,371</u>	<u>16,898,626</u>	<u>110,134,985</u>
Expenditures charged to appropriations:				
Culture and recreation	7,276,175	459,411	(1,027,895)	6,707,691
Economic and social development	4,042,183	1,836,500	(2,061,247)	3,817,436
Education	2,123,170	-	4,392	2,127,562
General government	27,695,276	2,518,903	14,478,141	44,692,320
Capital outlays	1,254,317	-	1,294,683	2,549,000
Health and welfare	4,455,764	-	(185,118)	4,270,646
Housing	766,453	-	(32,945)	733,508
Sanitation and environmental	7,073,516	-	5,584,328	12,657,844
Public safety	7,811,401	554,565	(705,211)	7,660,755
Public works	13,228,141	8,810,992	(8,042,330)	13,996,803
Transfer out	3,329,592	-	7,591,828	10,921,420
Total charges to appropriations	<u>79,055,988</u>	<u>14,180,371</u>	<u>16,898,626</u>	<u>110,134,985</u>
Excess of resources over appropriations	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

- The city council amended the budget during the year by \$14,180,371 mainly by unreserved resources from prior year.

	Municipal Legislative Resolution No.				Total
	05B-25	05B-34	2006-45	2006-55	
Expenditures charged to appropriations:					
Culture and recreation	\$ 191,500	\$ 40,000	\$ 138,950	\$ 88,961	\$ 459,411
Economic and social development	16,000	27,500	673,000	1,120,000	1,836,500
General government	286,300	1,268,870	838,733	125,000	2,518,903
Public safety	-	285,000	269,565	-	554,565
Public works	517,400	4,637,316	1,304,926	2,351,650	8,810,992
Total charges to appropriations	<u>\$ 1,011,200</u>	<u>\$ 6,258,686</u>	<u>\$ 3,224,874</u>	<u>\$ 3,685,611</u>	<u>\$ 14,180,371</u>

- Additional resources were accounted for by \$16,898,626, including the newly adopted sales tax income by \$7,515,740. These were transfers from and to other funds that increased the General Fund budget.

Actual transactions generated an excess of resources over appropriations of \$9,997,023 due to the following:

- Actual collections increased \$1,785,658 (1%), primary by an increase in collection on volume of business and intergovernmental revenues
- Actual disbursements decreased by \$8,211,365 (7%), primary by a decrease in general government transfer to other funds.

Proprietary Funds. The Municipality's proprietary funds provide the same type of information found in the government-wide statements but in more detail. Unrestricted net assets of the Community Development Bank at the end of the fiscal year amounted to \$3,682,891, and those of the Multi-tenant Fund equaled \$1,935,196. The total increase (reduction) in net assets for both funds was (\$108,786) and \$780,622 respectively. Other factors concerning the finances of these funds have already been addressed in the discussion of the Municipality's business-type activities.

Capital Asset and Debt Administration

Capital assets. The Municipality's capital assets for its governmental and business – type activities as of June 30, 2006, totals \$333,705,338 (net of accumulated depreciation). These assets include buildings, roads and bridges, land, machinery and equipment, park facilities, and vehicles.

Major capital asset transactions during the year include:

- Purchased new equipment for the Municipality as a whole
- Purchased new vehicles for Public Works Department motor pool
- Disposal of old equipment
- Operating lease contract of the Fine Arts Center
- Addition of construction in progress for infrastructure, buildings and facilities

The Municipality's Capital Assets
(net of depreciation)
Figure 5

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Land	\$ 36,449,098	\$ 33,185,551	\$ 2,982,654	\$ 2,026,954	\$ 39,431,752	\$ 35,212,505
Buildings and system	8,357,237	8,790,659	3,670,289	2,939,720	12,027,526	11,730,379
Facilities	27,001,167	26,100,042	-	-	27,001,167	26,100,042
Machinery and equipment	14,103,069	12,865,186	32,413	34,492	14,135,479	12,899,678
Infrastructure	154,273,270	153,716,992	-	-	154,273,273	153,716,992
Works of art	2,685,541	2,600,941	-	-	2,620,541	2,600,941
Construction in progress	83,360,600	71,304,136	790,000	45,723	84,150,600	71,349,859
Total	\$ 326,229,982	\$ 308,563,507	\$ 7,475,356	\$ 5,046,889	\$ 333,640,338	\$ 313,610,396

Additional information on the Municipality's capital assets can be found in note 6 of the Basic Financial Statements.

Major additions to constructions in progress (disbursements of more than \$310,000) as of June 30, 2006 are as follows:

Project	Amount
Honor al Río	\$ 2,305,646
Portal del Este	1,456,809
Casa del Ajedrez	739,979
Parks and recreational areas	633,601
Eco. Plaza Barrio Borrinquen	570,798
Water supply Bo. Tomás de Castro	553,343
Water supply Bo. La Unión	491,342
Bo. Morales (relocation)	349,033
Muñoz Marín Ave sewer system	332,617
Parque Criollo	330,543
Other Water supply system	313,728

Long-term Debt. As of June 30, 2006, The Municipality had total bonded debt outstanding of \$155,587,725 all of which is debt backed by the full faith and credit of the Municipality.

The Municipality's Outstanding Debt

General Obligation Bonds

Figure 6

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
General obligation bonds	\$ 101,853,030	\$ 82,882,197	\$ 489,871	\$ 544,105	\$ 102,342,901	\$ 83,426,302
Federal loans and notes	9,560,000	10,470,000	-	-	9,560,000	10,470,000
Special loans	43,684,824	25,175,858	-	-	43,684,824	25,175,858
Total	\$ 155,097,854	\$ 118,528,055	\$ 489,871	\$ 544,105	\$ 155,587,725	\$ 119,072,160

The Municipality's total debt increased by \$36,515,565 (30 percent) during the past fiscal year, primarily due to the \$24,175,000 bond anticipation notes issued for infrastructure development and the \$20,090,000 issued in special loans for infrastructure development.

The Commonwealth of Puerto Rico limits the amount of general obligation debt that a unit of government can issue to 10 percent of the total assessed value of taxable property located within that government's boundaries. The total legal debt margin for the Municipality is approximately \$120,000,000. The Municipality has \$10,075,000 in bonds authorized issued, but not yet collected as of June 30, 2006.

Additional information regarding the Municipality's long-term debt can be found in note 7 beginning on page 50 of this audited financial report.

Economic Factors and Budgets and Rates

Summary of Local Economy

Caguas is the fifth largest City in Puerto Rico, out of 78 municipalities, accounting for roughly 3.7% of the Commonwealth's population. The Islands' 10% largest commercial centers of the are located in Caguas. The City is situated in the heart of Puerto Rico, at the intersection of three major highways, PR 1, PR 52, and PR 30. Its Statistical Area includes the communities of: Bairoa, Beatriz, Cañaboncito, Cañabon, Borinquen, Pueblo, San Antonio, San Salvador, Tomás de Castro, Turabo.

The largest employers in Caguas are the State government, the Municipal government, Pfizer, Mova, Avon, Walmart, Sams Club and Amigo Supermarket retail chain, Banco Popular, San Pablo-HIMA Hospital, Mylan, St. Jude Medical.

The City's economy has an industry composition somewhat similar to the rest of the island's largest Municipalities. In the 1960s textile's manufacturing and agriculture made up the largest amount of the local economy, but by the mid seventies the manufacturing share of employment had declined to a lower percentage.

Major Industries and Services (including government)

Government Services: The governmental service is the largest source of employment in the Municipality, accounting for the largest amount of the civilian employment in FY/06. This sector had a moderate grow at city level but it is being reduced at the State level since the last quarter of the fiscal year due to the economical weakness of the State. It is a diverse sector that includes jobs in the areas of education, electric power service, water supply, police, public works, culture and recreation, health, legal service and others.

Health Services: As a major regional medical center, the medical services industry is one of the largest employers in the area. It includes HIMA-San Pablo Hospital and the former Regional Hospital, now named San Juan Bautista, operated by the private sector. The health services industry had been one of the fastest growing sectors in the Caguas area. Even with recent uncertainties regarding health care financing, particularly the governmental health care program, its growth has continued at a rapid pace.

Trade (retail and wholesale): The trade sector is the strongest growing sector in the area. Many major national chains such as Walmart, Costco, Walgreens have expanded into the area and general growth and low interest rates have helped maintain relatively stable levels of consumer spending.

City Employment (in thousands)

NAICS CATEGORY	
Total Employment (does not include military)	52.296
Natural Resources and Mining and Construction	0.475
Manufacturing	8.001
Trade, Transportation, and Utilities	15.862
Information	0.952
Financial Activities	0.940
Aggregate of Services	26.230
Professional and Business Services	4.624
Educational and Health Services	3.156
Leisure and Hospitality	3.846
Other Services	1.215
Government	2.500
MILITARY	0.300

Source: Federal Department of Labor

Manufacturing - Pharmaceutical and Medical Devices and Technology:

Caguas pharmaceutical products and medical devices manufacturing sector accounts for a very important amount of employment of the private sector. Investments made by Mylan, Inc. a generic pharmaceutical manufacturer and other high tech firms are helping to create a critical mass of activity in Caguas that is expected to attract the interest of other firms including competitors, suppliers, and customers.

Construction: The construction in the private sector is a source of economic growth in Caguas. Employment and gross receipts in construction has been growing consistently during the last eight years with Hacienda San José and Los Prados developments - located at both sides of Jardín Criollo - and other multi and single family developments. During this year Los Prados continues expending as well as other developments such as Bosque Verde, Estancias del Bosque, Mansiones de Ciudad Jardín, River Park and other seven single-family housing developments. Actual capital investments in those projects reach \$462 millions and actual investment in social interest projects of single and multi- family developments exceeds \$40 millions for a total investment of more than \$500 millions. Social interest projects include 238 units for the elderly and 329 for low and moderate-income families.

Low interest rates and stable or reduced prices for much of the period helped fuel the growth. The lower priced homes also allowed many potential apartment dwellers to purchase houses. This is part of the reason the number of multi-family units permitted has been limited. Even with the large number of single-family units, the total number of units is far short of the peaks experienced in the 1970s and 1980s. The value of construction permits per home increased by 27% for FY/05 following an increase of 7% in FY/04. This means that even though the number of residential permits slightly declined in FY/05, the total value of permits increased.

Budget Highlights for the Fiscal Year Ending June 30, 2007

Governmental Activities: Property taxes (benefiting from residential and industrial developments), city tax, and revenues from permits and fees are expected to lead the increase in revenue projections by 16 percent (without considering any inter-fund transfer). The Municipality will use these increases in revenues to finance programs currently in place.

Budgeted expenditures in the General Fund are expected to rise approximately 16% to \$107,730,616. The largest increments are in employee compensation, including funding compensation and benefits adjustments, Capital Outlays and Public Works.

Requests for Information

This report is designed to provide an overview of the Municipality's finances for those with an interest in this area. Questions concerning any of the information found in this report or requests for additional information should be directed to: Municipality of Caguas, Office of the Mayor, P.O. Box 907, Caguas, Puerto Rico, 00726-0907, or <http://www.caguas.gov.pr>.

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Net Assets

June 30, 2006

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 75,021,382	\$ 4,253,016	\$ 79,274,398
Cash with fiscal agent	16,846,301	-	16,846,301
Volume of business tax receivables	14,675,106	-	14,675,106
Sales taxes receivables	2,130,517	-	2,130,517
Intergovernmental receivables	17,568,373	-	17,568,373
Federal grant receivables	3,957,277	790,000	4,747,277
Rent and other services charge receivables	1,635,096	15,337	1,650,433
Internal balances	909,406	(909,406)	-
Total current assets	<u>132,743,458</u>	<u>4,148,947</u>	<u>136,892,405</u>
Noncurrent assets:			
Loan receivable, net	-	1,562,614	1,562,614
Capital assets, net	<u>326,229,982</u>	<u>7,475,356</u>	<u>333,705,338</u>
Total noncurrent assets	<u>326,229,982</u>	<u>9,037,970</u>	<u>335,267,952</u>
Total assets	<u>\$ 458,973,440</u>	<u>\$ 13,186,917</u>	<u>\$ 472,160,357</u>

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Net Assets (continued)

June 30, 2006

	Governmental Activities	Business-Type Activities	Total
LIABILITIES			
Current liabilities:			
Accounts payable	\$ 11,538,627	\$ 393,903	\$ 11,932,530
Deferred volume of business tax revenue	29,428,524		29,428,524
Deferred intergovernmental revenue	3,425,000		3,425,000
Bonds and notes payable, current	8,483,033	96,320	8,579,353
Accrued compensated absences, current	987,000	-	987,000
Accrued legal claims, current	1,762,664	-	1,762,664
Due to other governments	658,369	-	658,369
Advance deposits	1,122,622	-	1,122,622
Total current liabilities	<u>57,405,839</u>	<u>490,223</u>	<u>57,896,062</u>
Noncurrent liabilities:			
Bonds and notes payable, noncurrent	146,614,821	393,551	147,008,372
Accrued compensated absences, noncurrent	7,685,108	-	7,685,108
Accrued legal claims, noncurrent	2,319,098	-	2,319,098
Other accrued liabilities	981,604	-	981,604
Total noncurrent liabilities	<u>157,600,631</u>	<u>393,551</u>	<u>157,994,182</u>
Total liabilities	<u>215,006,470</u>	<u>883,774</u>	<u>215,890,244</u>
Net assets:			
Invested in capital assets, net of related debt	184,676,300	7,813,633	192,489,933
Restricted for:			
Housing programs	2,961,412	-	2,961,412
Youth and children programs	1,004,969	-	1,004,969
Capital projects	29,629,036	-	29,629,036
Debt service	16,846,301	489,871	17,336,172
Other special purposes	2,501,819	1,562,614	4,064,433
Unrestricted	6,347,133	2,437,025	8,784,158
Total net assets	<u>243,966,970</u>	<u>12,303,143</u>	<u>256,270,113</u>

See notes to financial statements

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Activities
For the Fiscal Year Ended June 30, 2006

Functions Programs	Expenses	Revenues			Net (Expense) Revenue and Changes in Net Assets		
		Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total
Governmental activities:							
General government	\$ 38,310,363	\$ 1,885,100	\$ 10,832,132	\$ -	\$ (25,593,131)	\$ -	\$ (25,593,131)
Public safety	8,797,955	73,773	138,545	-	(8,585,637)	-	(8,585,637)
Public works	24,469,027	-	-	6,164,373	(18,304,654)	-	(18,304,654)
Culture and recreation	8,276,237	-	-	-	(8,276,237)	-	(8,276,237)
Health and wealthfare	9,295,701	903,191	4,400,329	-	(3,992,181)	-	(3,992,181)
Economic and social development	4,133,619	577,071	-	-	(3,556,548)	-	(3,556,548)
Housing	12,633,171	2,217,324	14,470,858	-	4,055,011	-	4,055,011
Sanitation and environmental	11,737,150	-	250,000	-	(11,487,150)	-	(11,487,150)
Education	15,234,980	-	12,945,158	-	(2,289,822)	-	(2,289,822)
Debt service payments	7,767,626	-	-	-	(7,767,626)	-	(7,767,626)
Total governmental activities	140,655,829	5,656,459	43,037,022	6,164,373	(85,797,975)	-	(85,797,975)
Business-type activities:							
Community Development Bank	234,539	113,903	-	-	-	(120,636)	(120,636)
Multitenant	128,914	231,128	-	653,223	-	755,437	755,437
Total Business-type activities	363,453	345,031	-	653,223	-	634,801	634,801
General revenues:							
Property taxes					52,535,437	-	52,535,437
Volume of business taxes					27,906,137	-	27,906,137
Sales taxes					8,902,250	-	8,902,250
Licenses and permits					9,374,513	-	9,374,513
Interest and investment income					2,369,454	37,035	2,406,489
Total general revenues					101,087,791	37,035	101,124,826
Change in net assets					15,289,816	671,836	15,961,652
Net assets - beginning (as previously reported)					150,019,996	10,080,729	160,100,725
Prior period adjustments					78,657,158	1,550,578	80,207,736
Net assets - beginning (as restated)					228,677,154	11,631,307	240,308,461
Net assets - ending					\$ 243,966,970	\$ 12,303,143	\$ 256,270,113

See notes to financial statements

MUNICIPALITY OF CAGUAS, PUERTO RICO

Governmental Funds Balance Sheet
June 30, 2006

	General	Housing and Rental Program	Public Residential Administration	Head Start Youth and Children Programs	Capital Projects	Debt Service	Legislative	Other Special Revenue	Total Governmental Funds
ASSETS									
Cash and investments	\$ 26,818,123	\$ 6,787,233	\$ 194,016	\$ 1,262,454	\$ 34,721,275	\$ -	\$ 1,154,475	\$ 4,083,806	\$ 75,021,382
Cash with fiscal agent	-	-	-	-	-	16,846,301	-	-	16,846,301
Volume of business tax receivables	14,675,106	-	-	-	-	-	-	-	14,675,106
Sales tax receivables	2,130,517	-	-	-	-	-	-	-	2,130,517
Intergovernmental receivables	14,143,373	-	-	-	-	-	3,425,000	-	17,568,373
Federal grants receivables	-	2,440,012	-	781,808	305,487	-	-	429,970	3,957,277
Due from other funds	8,371,200	-	-	-	-	-	-	-	8,371,200
Rent and other services charge receivables	1,476,170	-	-	-	154,755	-	-	4,171	1,635,096
Total assets	\$ 67,614,489	\$ 9,227,245	\$ 194,016	\$ 2,044,262	\$ 35,181,517	\$ 16,846,301	\$ 4,579,475	\$ 4,517,947	\$ 140,205,252

MUNICIPALITY OF CAGUAS, PUERTO RICO

Governmental Funds Balance Sheet (continued)

June 30, 2006

	General	Housing Rental Program	Public Residential Administration	Head Start Youth and Children Programs	Capital Projects	Debt Service	Legislative	Other Special Revenue	Total Governmental Fund
LIABILITIES AND FUND BALANCES									
Liabilities:									
Accounts payable and accrued liabilities	\$ 5,197,145	\$ 646,328	\$ 91,700	\$ 261,213	\$ 4,286,940	\$ -	\$ 382,274	\$ 673,027	\$ 11,538,627
Due to other governments	658,369	-	-	-	-	-	-	-	658,369
Due to other funds	-	3,460,301	16,141	778,080	1,579,125	-	285,046	1,343,101	7,461,794
Deferred volume of business taxes	29,428,524	-	-	-	-	-	-	-	29,428,524
Deferred federal grant revenues	-	1,564,735	-	-	173,571	-	-	-	1,738,306
Deferred intergovernmental advanced deposits	1,122,622	-	-	-	-	-	3,425,000	-	3,425,000
Total liabilities	36,406,660	5,671,364	107,841	1,039,293	6,039,636	-	4,092,320	2,016,128	55,373,242
Fund Balances									
Reserve for:									
Reserved for encumbrances	16,293,914	-	-	-	-	-	-	-	16,293,914
Reserved for housing programs	-	3,555,881	86,175	-	-	-	-	-	3,642,056
Reserved for youth and children programs	-	-	-	1,004,969	-	-	-	-	1,004,969
Reserved for debt service	-	-	-	-	-	16,846,301	-	-	16,846,301
Reserved for capital projects	-	-	-	-	29,141,881	-	487,155	-	29,629,036
Reserved for special projects	-	-	-	-	-	-	-	2,501,819	2,501,819
Unreserved	14,913,915	-	-	-	-	-	-	-	14,913,915
Total fund balances	31,207,829	3,555,881	86,175	1,004,969	29,141,881	16,846,301	487,155	2,501,819	84,832,010
Total liabilities and fund balances	\$ 67,614,489	\$ 9,227,245	\$ 194,016	\$ 2,044,262	\$ 35,181,517	\$ 16,846,301	\$ 4,579,475	\$ 4,517,947	\$ 140,205,252

See notes to financial statements

MUNICIPALITY OF CAGUAS

Reconciliation of Fund Balance of Governmental Funds
to Net Assets of Governmental Activities
June 30, 2006

Fund balance per Fund statements	\$ 84,832,010
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resource and not reported in the funds	326,229,982
Other federal grants that are economic resources in the governmental activities are deferred revenues in the governmental funds since they do not involve the use of current financial resources	1,738,306
Other long-term liabilities, such as accrued compensated absences, litigations and other contingencies are not available to pay for current year expenditures and therefore not reported in the funds	(13,735,474)
General obligation bonds, special and federal loans are not due and payable in the current period and therefore not reported in the funds	<u>(155,097,854)</u>
Net assets of governmental activities	<u>\$ 243,966,970</u>

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Fiscal Year Ended June 30, 2006

	General	Housing and Rental Programs	Public Residential Administration	Head Start Youth and Children Programs	Capital Projects	Debt Service	Legislative	Other Special Revenue	Totals
Revenues :									
Property taxes	\$ 35,939,233	\$ -	\$ -	\$ -	\$ -	\$ 16,596,204	\$ -	\$ -	\$ 52,535,437
Volume of business taxes	27,906,137	-	-	-	-	-	-	-	27,906,137
Sales taxes	8,902,250	-	-	-	-	-	-	-	8,902,250
Licenses and permits	9,361,812	-	-	-	12,901	-	-	45	9,374,558
Federal grants	-	9,332,948	959,698	14,630,564	4,992,200	-	-	3,077,927	32,993,337
Fines and penalties	73,773	-	-	-	-	-	-	-	73,773
Interest and investment income	2,246,386	55,127	-	12,159	-	-	31,325	24,749	2,369,746
Intergovernmental	10,832,132	2,450,000	-	-	4,588	-	2,667,467	452,726	16,406,913
Parking lot fees	186,009	-	-	-	18,000	-	-	96,323	300,332
Rent	291,347	-	-	-	170,651	-	-	44,811	506,809
Other	1,699,091	2,217,324	-	14,888	-	-	-	843,492	4,774,795
Total revenues	97,437,970	14,055,399	959,698	14,657,611	5,198,340	16,596,204	2,896,792	4,540,073	156,144,087
Expenditures									
General government	36,821,338	-	-	-	-	-	-	-	36,821,338
Public safety	7,544,794	-	-	-	-	-	8,400	921,305	8,474,499
Public works	11,908,702	-	-	-	1,716,516	-	326,232	668,248	14,619,698
Culture and recreation	6,498,929	-	-	-	1,196,764	-	-	309,900	8,005,593
Health and welfare	3,989,954	-	-	1,493,978	183,771	-	328,457	2,956,494	8,952,654
Economic and social development	3,583,443	-	-	-	238,734	-	59,893	157,014	4,039,084
Housing	731,704	9,858,874	860,869	-	410,764	-	-	-	11,862,211
Sanitation and environmental	11,393,146	-	-	-	-	-	-	55,136	11,448,282
Education	2,067,093	-	-	12,583,436	20,008	-	-	403,336	15,073,873
Capital outlays	6,392,706	680,644	12,654	551,102	16,600,366	-	2,126,934	1,162,560	27,526,966
Debt service payments	-	-	-	-	-	-	-	-	-
Principal	-	-	-	-	-	7,695,033	-	-	7,695,033
Interest	-	-	-	-	-	7,767,626	-	-	7,767,626
Total expenditures	90,931,809	10,539,518	873,523	14,628,516	20,366,923	15,462,659	2,849,916	6,833,993	162,286,857

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Revenues, Expenditures and Changes in Fund Balances-(continued)
 Governmental Funds
 For the Fiscal Year Ended June 30, 2006

	General	Housing and Rental Programs	Public Residential Administration	Head Start Youth and Children Programs	Capital Projects	Debt Service	Legislative	Other Special Revenue	Totals
Other financing sources (uses)									
Proceeds from debt issuance	10,075,000	-	-	-	32,050,000	-	-	-	42,125,000
Property taxes transferred from debt service fund	4,000,000	-	-	-	-	(4,000,000)	-	-	-
Interest transferred from debt service fund	407,673	-	-	-	-	(407,673)	-	-	-
Operating transfer in	-	40,000	-	11,500	4,919,466	6,558,370	75,000	2,480,678	14,085,014
Operating transfer out	(10,921,420)	-	-	-	(3,163,594)	-	-	-	(14,085,014)
Other financing sources, net	<u>3,561,253</u>	<u>40,000</u>	<u>-</u>	<u>11,500</u>	<u>33,805,872</u>	<u>2,150,697</u>	<u>75,000</u>	<u>2,480,678</u>	<u>42,125,000</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	<u>10,067,414</u>	<u>3,555,881</u>	<u>86,175</u>	<u>40,595</u>	<u>18,637,289</u>	<u>3,284,242</u>	<u>(76,124)</u>	<u>386,758</u>	<u>35,982,230</u>
Fund balances at beginning of year (as previously reported)	26,864,057	3,184,899	965,481	4,222,237	22,665,933	13,562,059	563,279	2,081,279	73,929,224
Prior period adjustment	(5,543,642)	(3,164,899)	(965,481)	(3,257,863)	(12,161,341)	-	-	33,782	(25,079,444)
Fund balances at beginning of year (as restated)	<u>21,140,415</u>	<u>-</u>	<u>-</u>	<u>964,374</u>	<u>10,504,592</u>	<u>13,562,059</u>	<u>563,279</u>	<u>2,115,061</u>	<u>48,849,780</u>
Fund balances at end of year	<u>\$ 31,207,829</u>	<u>\$ 3,555,881</u>	<u>\$ 86,175</u>	<u>\$ 1,004,969</u>	<u>\$ 29,141,861</u>	<u>\$ 16,846,301</u>	<u>\$ 487,155</u>	<u>\$ 2,501,819</u>	<u>\$ 84,832,010</u>

Dr. Cruz 15/06/07

*- 5,543,642
 304,017
 5,039,625 ajuste*

MUNICIPALITY OF CAGUAS, PUERTO RICO

Reconciliation of the Statement of Revenues, Expenditures and
 Changes in Fund Balances of Governmental Funds
 to the Statement of Activities
 Fiscal Year Ended June 30, 2006

Net change in fund balance - total governmental funds	\$	35,982,230
Amounts reported in the statement of activities 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 as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.		
		17,711,895
General long-term debt proceeds provide current financial resources to governmental funds, but issuing debt increases long term liabilities in the statement of net assets. Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long term liabilities in the statement of net assets. This is the amount by which proceeds exceed or are below the repayments		
		(34,429,967)
Some revenues and expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as revenues and expenditures in the governmental funds.		
		<u>(3,974,342)</u>
Change in net assets of governmental activities	\$	<u>15,289,816</u>

See notes to financial statements

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Revenues and Expenditures
 Budget and Actual- General Fund
 Non GAAP Budgetary Basis
 Year Ended June 30, 2006

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual amounts in the budgetary basis</u>	<u>Variance Favorable (Unfavorable)</u>
Resources:				
Property taxes	\$ 34,648,877	\$ 34,648,877	\$ 35,939,233	\$ 1,290,356
Volume of business taxes	24,250,000	24,250,000	27,906,137	3,656,137
Sales taxes	-	7,515,140	8,902,250	1,387,110
Fines and penalties	1,000,000	1,000,000	73,773	(926,227)
Interest and investment income	1,000,000	1,000,000	2,246,386	1,246,386
Intergovernmental	8,325,071	8,325,071	10,832,132	2,507,061
Licenses and permits	9,228,000	9,228,000	9,361,612	133,612
Parking lot fees	174,919	174,919	186,009	11,090
Rent	339,821	339,821	291,347	(48,474)
Other resources	89,300	23,653,157	16,181,764	(7,471,393)
Amounts available for appropriation	<u>\$ 79,055,988</u>	<u>\$ 110,134,985</u>	<u>\$ 111,920,643</u>	<u>\$ 1,785,658</u>
Expenditures charged to appropriations:				
Culture and recreation	7,276,175	6,707,691	6,684,159	23,532
Economic and social development	4,042,183	3,817,436	3,815,840	1,596
Education	2,123,170	2,127,562	2,126,464	1,098
General government	27,695,276	44,692,320	36,553,993	8,138,327
Capital outlays	1,254,317	2,549,000	2,532,903	16,097
Health and welfare	4,455,764	4,270,646	4,266,836	3,810
Housing	766,453	733,508	731,704	1,804
Sanitation and environmental	7,073,516	12,657,844	12,653,374	4,470
Public safety	7,811,401	7,660,755	7,658,611	2,144
Public works	13,228,141	13,996,803	13,978,316	18,487
Transfer out	3,329,592	10,921,420	10,921,420	-
Total charges to appropriations	<u>79,055,988</u>	<u>110,134,985</u>	<u>101,923,620</u>	<u>8,211,365</u>
Excess of resources over appropriations	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 9,997,023</u>	<u>\$ 9,997,023</u>

See notes to the financial statements

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Net Assets
Proprietary Funds
June 30, 2006

	Community Development Bank	Multitenant Funds	Totals
Assets			
Current Assets:			
Cash and cash equivalents	\$ 2,915,801	\$ 1,337,215	\$ 4,253,016
Rent receivable	-	15,337	15,337
Due from federal agency	-	790,000	790,000
Total current assets	<u>2,915,801</u>	<u>2,142,552</u>	<u>5,058,353</u>
Noncurrent Assets:			
Loans receivable, net	<u>1,562,614</u>	-	<u>1,562,614</u>
Capital assets:			
Land	-	2,982,654	2,982,654
Building and improvements	-	4,047,765	4,047,765
Equipment	33,603	2,144	35,747
Less: Accumulated depreciation	(30,969)	(349,841)	(380,810)
Construction in progress	-	790,000	790,000
Capital assets net	<u>2,634</u>	<u>7,472,722</u>	<u>7,475,356</u>
Total non-current assets	<u>1,565,248</u>	<u>7,472,722</u>	<u>9,037,970</u>
Total assets	<u>\$ 4,481,049</u>	<u>\$ 9,615,274</u>	<u>\$ 14,096,323</u>

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Net Assets (continued)
Proprietary Funds
June 30, 2006

	Community Development Bank	Multitenant Funds	Totals
Liabilities			
Current liabilities			
Notes payable (current portion)	\$ 96,320	\$ -	\$ 96,320
Due to other fund	-	909,406	909,406
Accounts payable and accrued liabilities	305,953	87,950	393,903
Total current liabilities	<u>402,273</u>	<u>997,356</u>	<u>1,399,629</u>
Noncurrent liabilities:			
Notes payable (net of current portion)	<u>393,551</u>	-	<u>393,551</u>
Total liabilities	<u>795,824</u>	<u>997,356</u>	<u>1,793,180</u>
Net assets			
Investment in capital assets (net of related debt)	2,334	6,682,722	6,685,056
Unrestricted	<u>3,682,891</u>	<u>1,935,196</u>	<u>5,618,087</u>
Total net assets	<u>3,685,225</u>	<u>8,617,918</u>	<u>12,303,143</u>
Commitments and contingencies	-	-	-
Total liabilities and net assets	<u>\$ 4,481,049</u>	<u>\$ 9,615,274</u>	<u>\$ 14,096,323</u>

See notes to financial statements

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Revenues, Expenses and Changes in Net Assets
 Proprietary Funds
 For the Fiscal Year Ended June 30, 2006

	Community Development Bank	Multitenant Funds	Totals
Operating revenues:			
Rent, interest on loans and origination fees	\$ 113,903	\$ 231,128	\$ 345,031
Operating expenses:			
Payroll	81,881	-	81,881
Depreciation	7,640	63,073	70,713
Professional fees	91,700	4,520	96,220
Bank service charges	3,025	-	3,025
Repairs and maintenance	-	59,913	59,913
Office supplies	3,168	-	3,168
Rent	19,200	-	19,200
Utilities	6,000	-	6,000
Other	12,675	1,408	14,083
Total operating expenses	<u>225,289</u>	<u>128,914</u>	<u>354,203</u>
Income (loss) before contributions and transfers	<u>(111,386)</u>	<u>102,214</u>	<u>(9,172)</u>
Non-operating revenues (expenses)			
Interest income	11,850	25,185	37,035
Interest expense	(9,250)	-	(9,250)
Total non-operating revenues (expenses)	<u>2,600</u>	<u>25,185</u>	<u>27,785</u>
Income (loss) before contributions and transfers	<u>(108,786)</u>	<u>127,399</u>	<u>18,613</u>
Contributions:			
Capital contribution from Federal Government	-	653,223	653,223
Changes in net assets	<u>(108,786)</u>	<u>780,622</u>	<u>671,836</u>
Net assets at beginning of fiscal year			
(as previously reported)	3,794,011	6,286,718	10,080,729
Prior period adjustment	-	1,550,578	1,550,578
Net assets at beginning of fiscal year (restated)	<u>3,794,011</u>	<u>7,837,296</u>	<u>11,631,307</u>
Net assets at end of fiscal year	<u>\$ 3,685,225</u>	<u>\$ 8,617,918</u>	<u>\$ 12,303,143</u>

See notes to financial statements

MUNICIPALITY OF CAGUAS, PUERTO RICO

Statement of Cash-Flows
Proprietary Funds
June 30, 2006

	Community Development Bank	Multitenant Funds	Totals
Cash flows from operating activities:			
Receipts from customers	\$ 113,903	\$ 215,791	329,694
Payments to suppliers	(118,927)	(109,211)	(228,138)
Payments to employees	(81,881)	-	(81,881)
Net cash provided by (used in) operating activities	<u>(86,905)</u>	<u>106,580</u>	<u>19,675</u>
Cash flows from capital and related financing activities:			
Capital assets investments	(434)	(653,223)	(653,657)
Capital contributions from Federal Government		653,223	653,223
Increase in amount due from Federal Government		(574,585)	(574,585)
Principal paid on capital debt	(70,135)	-	(70,135)
Interest paid on capital debt	(9,250)	-	(9,250)
Net cash provided by (used in) capital and financing activities	<u>(79,819)</u>	<u>(574,585)</u>	<u>(654,404)</u>
Cash flows from non-capital financing activities:			
Increase in loan from general fund	-	549,400	549,400
Cash flows from investing activities:			
Principal collections of loans	1,821,611	-	1,821,611
Loans disbursed	(428,500)		(428,500)
Interest income	11,850	25,185	37,035
Net cash provided by investing activities	<u>1,404,961</u>	<u>25,185</u>	<u>1,430,146</u>
Net increase (decrease) in cash	1,238,237	106,580	1,344,817
Cash at beginning fiscal year	<u>1,677,564</u>	<u>1,230,635</u>	<u>2,908,199</u>
Cash at end fiscal year	<u>\$ 2,915,801</u>	<u>\$ 1,337,215</u>	<u>\$ 4,253,016</u>
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:			
Adjustments to reconcile operating income (loss) to net cash provided in (used) in operating activities:			
Operating income (loss)	\$ (111,386)	\$ 102,214	\$ (9,172)
Depreciation	7,640	-	7,640
Increase in accounts payable	16,841	-	16,841
(Increase) decrease in rent receivable	-	4,366	4,366
Net cash provided by (used in) operating activities	<u>\$ (86,905)</u>	<u>\$ 106,580</u>	<u>\$ 19,675</u>

See notes to financial statements

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements
June 30, 2006

Note 1 - Summary of significant accounting policies

The Municipality of Caguas (the Municipality), founded in 1894, is a municipality of the Commonwealth of Puerto Rico. It is governed by a Major and a 16 member Municipal Assembly elected for a four-year term. The Municipality provides services to its residents in the areas of health, public works, education, public safety, urban development, economic development, culture and recreation, and other services.

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America.

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 of the Governmental Accounting Standards Board (GASB). 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 government appoints a voting majority of the entity's governing body and if either one of the following conditions exist; the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. Based on the above criteria the Municipality does not have component units to include within its reporting entity.

In June 1999, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 34 Basic Financial Statements – and Management's Discussion and Analysis - for State and Local Governments. GASB-34 significantly changed the way in which the Municipality reported its finances.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

GASB-34 established two bases for reporting financial information: government-wide financial statements and fund presentation. The government-wide financial statements method adopts the flow of economic resources measurement focus and accrual basis of accounting for both governmental activities and business-type activities. The basis for preparing fund financial statements is similar to conventional governmental financial statements except the focus for presentation is on major funds rather than fund types. Capital assets, including infrastructure assets, and depreciation charges are reported on the entity-wide perspective financial statements. The management's discussion and analysis information precedes the basis financial statements but is considered required supplementary information. Budgetary information is no longer presented in the financial statements but rather is presented as required supplementary information.

The Municipality implemented this statement in fiscal year ended June 30, 2003.

Basic Financial Statements GASB Statement No. 34

Government Wide Financial Statements:

The focus of the government wide financial statements is on the overall financial position and activities of the Municipality as a whole. The government wide financial statements will provide with the following:

- Present financial information about the overall government without presenting information about the individual funds or fund types.
- Differentiate between the Municipality's governmental activities and business type activities.
- Measure and present all financial balances and activities based on the economic resources measurement focus and the accrual basis of accounting.

The flow of economic resources measurement and accrual accounting are the basis upon which government wide financial statements are prepared. Under the flow of economic resources measurement focus and accrual basis of accounting, revenues are recognized when earned and expenses are incurred when incurred when these activities are related to exchange and exchange like activities. In addition, long-lived assets are capitalized and depreciated over their estimated economic lives.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

The government wide statements include the Statement of Net Assets and the Statement of Activities:

Statement of net assets:

Presentation of assets and liabilities – Assets and liabilities should be presented in the statement of net assets based on their relative liquidity. The liquidity of the assets is determined based their ability to be converted in cash and the absence of any restriction that might limit their conversion to cash. The liquidity of liabilities is based on maturity dates or expected payment dates.

Presentation of capital assets – The governmental entity should report all of its capital assets in the statement of net assets, based on their original historical cost. Capital assets that have been donated should be capitalized at their estimated fair value at the date of the receipt.

Presentation of long-term liabilities - Long-term liabilities include debts such as bonds, notes, and federal loans. In addition, operating liabilities such as compensated absences and claims must be reported in the statement of net assets.

Presentation of component of net assets - Net assets represent the difference between the Municipality's total assets and its total liabilities. The statement of net assets must identify the components of the net assets, namely (a) invested in capital assets, net of related debt; (b) restricted net assets; and (c) unrestricted net assets.

Invested in capital assets, net of related debt is the difference between capital assets (net of accumulated depreciation) and liabilities attributable to the acquisition, construction or improvement of those assets.

Restricted net assets arise if either of the following conditions exists: (a) externally imposed by creditor, grantors, contributors or laws and regulations of other governments or (b) imposed by law through constitutional provisions or enabling legislation.

Assets that are not classified as invested in capital assets (net of related debt) or restricted are included in the category of unrestricted net assets.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Statement of Activities:

The focus of the statement of activities is on the net cost of the various activities provided by the governmental entity. The difference between the expenses and revenues related to the specific activities, which identifies the extent to which each function of the Municipality draws from the general revenues of the Municipality or if it is self financing through service charges, intergovernmental and federal grants.

Revenues and other financing inflows – A fundamental concept in the presentation of the statement of activities is the identification of resources inflows to the Municipality that are related to specific programs and those that are general in nature. Revenues are divided in program revenues and general revenues.

Program revenues - Program revenues are those that are identified with an specific function, otherwise the revenues would not flow to the Municipality. As established before, program revenues are presented in the statement of activities as a subtraction of related program expenses in order to identify the net cost or benefit of a particular program. Program revenues are divided in charges for services, operating grants and contributions and capital grants.

General revenues – General revenues included resources that are not specifically related with a specific function, but that are used in the operation of the Municipality.

Expenses – The Municipality reports expenses, including depreciation expense by function. Direct expenses are those that are specifically associated with a service, program or department and are clearly identifiable to a particular function.

Generally, the cost (net of estimated salvage value) of capital assets should be depreciated over their estimated useful lives. Depreciation expense is reported as direct expense of the specific functional category with which the related capital asset has relationship.

Fund Financial Statements:

Fund based financial statements are included in order to demonstrate that restrictions imposed by statutes, regulations, or contracts have been followed. The Municipality has the following major funds:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Governmental funds - These financial statements have a short term emphasis and generally measure and account for cash and other assets that can easily be converted to cash and are used to account for the Municipality's expendable financial resources and the related liabilities. The measurement focus is upon determination of any changes in financial position. The Municipality's major funds are the following:

General fund

The general fund is used to account for all financial transactions, except those required to be accounted for in another fund.

Housing and Rental Programs

Account for current financial resources restricted mainly for housing rental programs to low and very low income family units. Resources are funded by the United States Department of Housing and Urban Development, mainly through the Section 8 Housing Voucher and Home Investment Partnership Programs.

Head Start Youth and Children Program

Account for current financial resources restricted for the education of pre-school aged children that are funded by the United States Department of Health and Human Services and the United States Department of Agriculture.

Capital Projects

Capital projects fund is used to account for financial resources to be used for the acquisition or construction of major capital facilities, other than those financed by proprietary funds.

Debt service funds

The debt service fund is used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest and related costs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Legislative funds

The legislative funds account the accumulation of resources approved by the Legislature of the Commonwealth of Puerto Rico designated for the investment of such in special projects related mainly with health and welfare, public works, economic development and others as requested by the Municipality's citizenship.

Public Residential Administration

On March 26, 2003, the Municipality entered into an Intergovernmental Management Agreement with the Puerto Rico Public Housing Administration (PRPHA). The purpose of the Agreement was to designate the Municipality to act as independent contractor for the PRPHA to manage, administer and operate the low income housing project denominated as José Gautier Benítez, under the United States Housing Act of 1937, as amended. The Project is located at State Road No. 1, behind Villa del Carmen Shopping Center, Caguas, Puerto Rico.

As part of the Agreement, the Municipality submits, on the 1st day of February of each year, an Annual Management Plan in which it delineates its proposed budgets for the year and any work to be performed in the Project.

The terms of the Agreement commenced on May 1st, 2003 (effective date) and shall expire at midnight on April 30th, 2005 (original term). The Agreement may be renewed by the PRPHA for additional periods of one year each, but not beyond April 30th, 2007

The Municipality operates the Program using fiscal periods beginning on July 1st and ending June 30th.

Other Special Revenue funds

Current financial resources used to account for the proceeds of specific revenue sources (other than debt service or capital projects) such as federal grants, that are legally restricted to expenditures for various specified purposes.

The financial statements of the governmental funds are the following:

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Statement of revenues, expenditures and changes in fund balance - Reports information about the inflows, outflows and balances of current financial resources of each major governmental fund for the fiscal year ended June 30.

Proprietary funds – Financial statements for proprietary funds are based on the flow of economic resources (measurement focus) and the accrual basis of accounting. They are used to account for activities, which are similar to operations in the private sector. The proprietary fund type consists of enterprise funds.

Enterprise funds

The enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent is that the cost of providing goods and services (including depreciation) be financed or recovered primarily through user charges, or where the Municipality has decided that periodic determination of revenues earned and expenses incurred is appropriate. The Municipality's enterprise funds follows:

Community Development Bank - Accounts for the economic resources designated mainly for the approval of loans for economic development, education and emergency in the benefit of the Caguas citizenship.

Multi-tenant Funds - Accounts the deposit of rental resources designated for the Municipality's normal operation other than those functions accounted in the general fund.

The financial statements of the proprietary funds are the following:

Statement of net assets or balance sheet - Assets and liabilities are presented in a classified format to distinguish between current and long term assets and liabilities.

Statement of revenues, expenditures and changes in fund net assets - Revenues and expenses are reported by distinguishing between operating and non-operating revenues and expenses.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Statement of cash flows - The primary purpose of the statement of cash flows is to provide relevant information about the cash receipts and disbursements of the Municipality during the fiscal year. The information of the statement of cash flows should help financial report users assess (a) Municipality's ability to generate future net cash flows; (b) ability to meet its obligation as they come due; (c) its needs for external financing; (d) the reasons for differences between operating income and associated cash receipts and disbursements and the effects on the entity's financial position of operating, capital and related financing activities, non-capital related financing activities and investment activities during the period.

Basis of accounting

The basis of accounting determines when the Municipality recognizes revenues and expenditures/expenses and related assets and liabilities.

Governmental fund types follow the modified accrual basis of accounting. Under this basis of accounting, revenues are recorded in the accounting period in which they become susceptible to accrual, that is, when they become both measurable and available. Available is defined as expected to be collected within the current period or soon enough thereafter to be used to pay liabilities of the current period.

In applying the susceptible to accrual concept to governmental revenues, there are essentially two types of revenues. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the Municipality; therefore, revenues are recognized based upon the expenditures incurred. In the other, monies are virtually unrestricted and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if the susceptible to accrual criteria are met.

The Municipality reports deferred revenue on its combined balance sheet. Deferred revenue arises when potential revenue does not meet both the measurable and available criteria for recognition in the current period. Deferred revenue also arises when the Municipality receives resources before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures.

In subsequent periods, when both revenue recognition criteria are met, or when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed from the combined balance sheet and revenue is recognized.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Licenses, permits, service charges, fines and forfeits and miscellaneous revenues are recorded as revenues on the cash basis, which includes amounts collected shortly after June 30. Investment income is recorded as revenue when received. The enterprise fund follows the accrual basis of accounting. Under the accrual basis, revenue is recognized when earned and expenses are recorded as liabilities when incurred, without regard to receipt or payment of cash.

Expenditures and related liabilities are generally recorded, except as described below, in the accounting period in which the liability is incurred. Expenditures and related liabilities for interest on long-term obligations, are recorded when due, except for interest due July 1st of the following year which is accounted for as paid on June 30. Vacation, sick leave, disallowances and litigation are recorded in the statement of net assets.

Budgetary accounting

The Municipality's annual budget is prepared on the budgetary basis of accounting and represents departmental appropriations recommended by the Mayor and approved by the Municipality's City Council prior to the beginning of the fiscal year. Budgetary control is maintained at the department level for each individual appropriation.

Amendments to the budget, and budgetary transfers related to personal expenditures, require the approval of the City Council. Non-capital encumbrances lapse at the end of the next fiscal year.

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 Statement of Revenues and Expenditures - Budget and Actual - General Fund is presented on the budgetary basis to enhance comparability.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

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

1. Encumbrances are considered as expenditures for budgetary purposes.
2. Prior year encumbrances settled during the year and recorded as expenditures for GAAP Basis.
3. Effect of GAAP basis accruals.
4. Effect of City Council resolutions due to budget readjustments, recognized as revenue during the year.

The following is reconciliation, of the differences between GAAP and the budgetary basis for the general fund excess of expenditures and other financing uses over revenues and other financing sources:

Change in fund balance as per Statement of Revenues, Expenditures and Change in fund balance (GAAP Basis)	\$10,067,414
Prior year's encumbrances settled during the current fiscal year	8,014,934
Current fiscal year encumbrances treated as current year expenditures for budgetary purposes	(8,085,325)
Municipality legislature resolutions	<u> -</u>
Excess of resources over appropriations - Non GAAP Budgetary Basis	<u>\$ 9,997,023</u>

Cash and investments

Substantially all cash balances are commingled in a deposit and checking accounts, certificates of deposits and several special purpose bank accounts, except for cash and investments restricted by law. Each fund records its equity interest in the pooled cash balance. The available cash balance in the general checking account beyond immediate needs is invested in interest-bearing deposits. Investment earnings are all credited to the general fund.

Investments are carried at fair market value. At June 30, 2006 the Municipality had an unrealized loss on investments of approximately \$ 8,498. Investments are composed of highly liquid U.S. Treasury Securities which are covered by the provisions of GASB Statement No. 31 "Accounting and Financial Reporting for Certain Investments and for External Investment Pools" therefore, the Municipality accounts for changes in the market value of its investments at the closing of the period.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Cash with fiscal agent reports property tax collections retained by the "Centro de Recaudaciones de Ingresos Municipales" (CRIM) and restricted for the payment of the Municipality's general obligations through the debt service fund.

Inter-fund transactions

The Municipality has the following types of transactions among funds:

Operating transfers - Transfers that are reported when incurred as "Operating transfers in" by the recipient fund and as "Operating transfers out" by the disbursing fund.

Receivables and payable - Transactions between funds outstanding at the end of the fiscal year are referred as due to/from other funds. The general fund provides services, at cost, to other funds. The amounts charged to other funds are treated as reductions in expenditures of the general fund.

Eliminations are made in the government wide statements of the amounts reported as inter-fund receivables as well as operating transfers, except for the net residual amounts due between governmental and business-type activities, which are reported as internal balances.

Capital assets

Capital assets acquired or constructed, whether owned by governmental activities or business-type activities are recorded and depreciated in the government-wide financial statements. No long-term capital assets or depreciation are shown in the governmental funds financial statements.

Capital assets, include public domain infrastructure (e.g., roads, bridges, sidewalks and other assets that are immovable and of value only to the Municipality). Capital assets are recorded at cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at the estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the capital asset or extend capital assets lives are not capitalized. Major improvements are capitalized and depreciated over the remaining useful lives of the related capital assets. Finally, major outlays for capital assets and improvements are capitalized as the projects are constructed.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

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

Facilities and recreational parks	120 to 720 months
Building and building improvements	60 to 360 months
Streets and roads	nil to 600 months
Personal property	36 to 180 months
Software	60 to 72 months

Compensated absences

Employees accrue vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated unpaid sick leave at their then current rate of pay, if the employee has at least 10 years of service with the Municipality. Total vested pay benefits accrued for compensated absences at June 30, 2006 amounts to \$8,672,108.

Long-term debt

The liabilities reported in the government-wide statements include the Municipality's general obligation bonds and notes for the realization of capital projects, and other long-term liabilities including vacation, sick leave, and litigation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Reserves of fund balance

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

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.

Debt service - Represents fund balance available to finance future debt service payments.

Capital projects - Represent fund balance available to finance future capital outlays and other public works projects.

Legislative – Represents fund balances available to finance projects approved by the Legislature of the Commonwealth of Puerto Rico for housing, culture an recreation, public works, economic development and other activities requested by the Municipality's citizenship.

Head Start Youth and Children programs – Represents fund balances available to finance activities of education and care of the eligible elderly population, mainly through the Head Start, Child Care and Child Care Food federal programs.

Housing projects – Represents fund balances available to finance activities oriented to the housing rent, acquisition, construction and rehabilitation for the Municipality's eligible citizenship.

Claims and judgments

The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund. The government wide financial statements include 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 2 - Annual revenues

Property taxes

The CRIM is responsible for the assessment of all real and personal property located within the Municipality of Caguas and for the levy, administration and collection of the corresponding taxes. The property tax is levied each year on the assessed value of the property at the beginning of the calendar year. Assessed values of real property are established at the estimated current value existing in the year 1957 and of personal property at the current value at the date of assessment.

Complete real property tax exoneration is granted by the Commonwealth of Puerto Rico on the first \$15,000 of the assessed valuation of owner occupied residential units. However, the Municipality receives the full amount levied, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. Complete exemption from personal property taxes up to an assessment of \$50,000 is granted to retailers with an annual volume of net sales under \$150,000. The Department of the Treasury instead of the property taxpayer becomes the source of payment in these cases.

The annual tax rate for fiscal year 2005 is 8.78% for real property and 6.58% for personal property of which 1.03% of both belongs to the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 6.00% and 4.00% respectively, represent the Municipality's basic property tax rate which is appropriated for general purposes and accounted in the general fund. Such amount is deposited by the CRIM in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.75% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

The Commonwealth also contributes an annual tax rate of .20% of each of the tax rates due to a discount granted by the state to the taxpayers.

Since the collection of property taxes from the taxpayers is under the administration of the CRIM, the Municipality records the revenues related to property taxes, net of the operational expenses allocated by the CRIM to the Municipality, when such revenues are reported by the CRIM. During the fiscal year ended June 30, 2006 the allocated expenses amounted to \$1,306,337.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

At the end of fiscal year, the amount receivable or payable arising from the fiscal year end settlement of actual property tax collections versus property tax advances made by the CRIM to the Municipality are reported as an increase or deduction of property tax revenue in the general fund, as applicable. Advances of property tax on (a) and (b) above, are recorded as revenues on the General Fund and Debt Service Fund, respectively.

Municipal license taxes

The Municipality imposes a volume of business tax pursuant to Act No. 82 of August 30, 1991, on all business entities, which operate within the Municipality, which are not exempt from the tax pursuant to the Industrial Incentives Act. The tax is based on gross revenues, as defined by law, computed at the rate of 1.50% for financial institutions and savings and loans associations, and .50% for all other business entities.

The minimum gross revenue to file the Volume of Business Tax Declaration is \$5,000 and the minimum tax payable is \$25. The date to file the Volume of Business Tax Declaration is April 15. The Municipality grants a five percent discount, if the taxes are paid on or before April 15. Otherwise, 50% of taxes payable must be paid within the first 15 days of each semester beginning with the first semester ending December 31.

Collections of volume of business tax revenues received mainly in April 15, are accounted as deferred revenues, since such collections have a time requirement and should be used starting July 1st of next fiscal year. In the next fiscal year, the deferred volume of business tax revenues are recognized as revenue, net of any credit or refunds payable to taxpayers.

Sales taxes

On February, 2005, the Municipal Legislature approved the Ordinance No. 05A-46, which defined the public policy of establishing a Municipal Citizen's Contribution (a sales tax) of 1% over retail sales inside the municipal jurisdiction. Said Ordinance was then amended on June 30, and October 31, 2005, to include the scope, limitations and administrative provisions for the management of the Contribution and some other tax-free items, respectively. A Ruling was also approved by the Mayor on September 1, 2005 to provide a better understanding of the Ordinances. The collection of said Contribution began on September 1, 2005. The Municipality, by means of the City's retailers, collected \$ 8,902,250 during the year ended June 30, 2006.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 3 - Cash, cash equivalents, and investments

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Commonwealth of Puerto Rico. The Municipality is also allowed to invest in bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the federal and Commonwealth laws. During the year, the Municipality invested its funds in interest bearing bank accounts, and certificates of deposit. The Municipality is subject to the following credit risks:

Custodial credit risk:

The Municipality is authorized to deposit only in institutions approved by the Department of the Treasury of the Commonwealth of Puerto Rico. Such deposits should be kept in separate accounts in the name of the Municipality. Under Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. During the year ended June 30, 2006, the Municipality invested its funds in bank accounts bearing interest.

At June 30, 2006 the Municipality had bank balances as follows:

Insured by the federal deposits insurance corporation	\$ 700,000
Collateralized by securities held by the pledging financial institution's trust department in the Corporation's name	<u>27,937,576</u>
Total	<u>\$ 28,637,576</u>

In addition, as of June 30 2006, the Municipality's custodial credit risk was approximately \$53 million, which is the bank balance of cash deposited at the Government Development Bank for Puerto Rico. These deposits are exempt from the collateral requirement established by the Commonwealth.

Interest rate credit risk:

At June 30, 2006, the Municipality maintains investments in debt securities with a fair market value of approximately \$4.2 million, that are secured by the Federal Government. Market values of such investments are very sensitive to the changes in the interest rates. At June 30, 2006, the Municipality had a risk of not recovering the market value of such investments if such investments are sold.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 4 - Intergovernmental revenues

Sources of intergovernmental revenues are primarily of governmental payments from the Commonwealth of Puerto Rico and "in lieu of tax" payments from certain quasi public corporations, such as Puerto Rico Electric Power Authority. The amount of contribution in lieu of tax for the year 2005-2006 was \$ 5,188,080.

Grants and subsidies received from the Commonwealth of Puerto Rico include, among others, subsidies through legislative appropriations mainly for capital improvements.

Note 5 - Interfund loans

Due from/to other funds

Interfund receivables and payables generally reflect temporary loans, billings for services provided and recovery of expenditures. Following is a summary of interfund assets and liabilities as of June 30, 2006:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
	Capital Project	\$1,579,125
	Legislative	285,046
	Head Start Program	778,080
	Housing and Rental	3,460,301
	Other Special Revenue	1,343,101
	Public Residential Administration	16,141
	Multi-tenant Funds	<u>909,406</u>
General		<u>\$8,371,200</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Transfers in/out

Inter-fund transfers in/out reflect the transfers of resources between from one fund to another without the attempt of recovering. Following is a summary of interfund transfers for the year ended June 30, 2006:

<u>Transferred In</u>	<u>Transferred Out</u>	<u>Amount</u>
Debt Service	Capital Project	<u>\$ 3,163,594</u>
Capital Project		4,919,466
Debt Service		3,394,776
Children		11,500
Housing and Rental		40,000
Legislative Fund		75,000
Other Special Revenue		<u>2,480,678</u>
	General Fund	<u>10,921,420</u>
Total		<u>\$ 14,085,014</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 6 - Capital assets

A summary of the activity of capital assets for governmental activities group follows:

	Balance June 30, 2005	Additions	Retirements	Transfers	Balance June 30, 2006
<u>Capital assets not being depreciated</u>					
Land and improvements	\$ 33,185,551	\$ 3,263,547	\$ -	\$ -	\$ 36,449,098
Construction in progress	71,304,136	20,104,583	-	(8,048,119)	83,360,600
Works of art and historical treasures	2,600,941	84,600	-	-	2,685,541
Total not being depreciated	<u>107,090,629</u>	<u>23,452,730</u>	<u>-</u>	<u>(8,048,119)</u>	<u>122,495,240</u>
<u>Other capital assets</u>					
Facilities and improvements	\$ 87,103,582	\$ -	\$ -	\$ 5,769,162	\$ 92,872,744
Buildings and improvements	13,488,737	-	-	75,501	13,564,237
Leasehold Improvements	17,115	-	-	-	17,115
Computer software	985,408	127,950	(1,274)	-	1,112,084
Roads and streets	181,916,368	-	-	2,203,456	184,119,824
Equipment and vehicles	28,020,489	3,946,286	(723,033)	-	31,243,742
Total Other capital assets	<u>\$ 311,531,698</u>	<u>\$ 4,074,236</u>	<u>\$ (724,307)</u>	<u>\$ 8,048,119</u>	<u>\$ 322,929,746</u>
<u>Accumulated depreciation</u>					
	Balance June 30, 2005	Depreciation Expense	Retirements	Transfers	Balance June 30, 2006
Facilities and improvements	\$ 61,003,540	\$ 4,868,038	\$ -	\$ -	\$ 65,871,577
Building and improvements	4,714,480	508,066	-	-	5,222,546
Leasehold Improvements	713	856	-	-	1,569
Equipment and vehicles	15,978,222	2,637,780	(677,911)	-	17,938,091
Computer software	162,489	153,152	(975)	-	314,666
Roads and streets	28,199,376	1,647,179	-	-	29,846,555
	<u>110,058,820</u>	<u>\$ 9,815,071</u>	<u>\$ (678,886)</u>	<u>\$ -</u>	<u>\$ 119,195,004</u>
Capital assets, net	<u>\$ 308,563,507</u>				<u>\$ 326,229,982</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

A summary of the activity of capital assets for business-type activities group follows:

	Balance at June 30, 2005	Additions	Retirements	Balance at June 30, 2006
Capital assets not being depreciated				
Land and improvements	\$ 2,982,654	\$ -	\$ -	\$ 2,982,654
Construction in progress	<u>136,777</u>	<u>653,223</u>	<u>-</u>	<u>790,000</u>
Total not being depreciated	<u>3,119,431</u>	<u>653,223</u>	<u>-</u>	<u>3,772,654</u>
Other capital assets				
Building and improvements	4,047,765	-	-	4,047,765
Equipment	<u>33,603</u>	<u>2,144</u>	<u>-</u>	<u>35,747</u>
Total other capital assets	<u>4,081,368</u>	<u>2,144</u>	<u>-</u>	<u>4,083,512</u>
Accumulated depreciation				
Building and improvement	285,767	63,073	-	348,840
Equipment	<u>24,330</u>	<u>7,640</u>	<u>-</u>	<u>31,970</u>
	<u>310,097</u>	<u>70,713</u>	<u>-</u>	<u>380,810</u>
Capital assets, net	<u>\$ 6,890,702</u>	<u>\$ 584,654</u>	<u>\$ -</u>	<u>\$ 7,475,356</u>

Depreciation expense for capital assets of governmental activities was charged to the following functions as follows:

General government	\$ 1,208,152
Public safety	123,398
Public works	7,181,525
Culture and recreation	154,199
Health and welfare	51,025
Economic and social development	37,810
Housing	731,582
Sanitation and environmental	189,117
Education	138,263
	<u>\$ 9,815,071</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 7 - General long - term debt

The legal debt margin of the Municipality is equal to 10% of the total assessment of property located within the Municipality. Total property assessments, based on information reported by the Municipal Revenue Collection Center amounted to \$1,205,013,264 of which \$603,980,438 and \$601,032,826 are real and personal property, respectively. All of the Municipality's long-term debt has been issued for the construction of capital projects in benefit of the citizenship.

Changes in general long - term debt of governmental activities for the fiscal year ended June 30, 2006 are summarized as follows:

	Bonds	Federal Loan and Notes	Special Loans	Totals
Balance at June 30, 2005	\$ 82,882,030	\$ 10,470,000	\$ 25,175,857	\$ 118,527,887
Payments	(5,204,000)	(910,000)	(1,581,033)	(7,695,033)
New debt issued	24,175,000	-	20,090,000	44,265,000
Balance at June 30, 2006	<u>\$ 101,853,030</u>	<u>\$ 9,560,000</u>	<u>\$ 43,684,824</u>	<u>\$ 155,097,854</u>

As of June 30, 2006, debt service requirements for the above long-term debt, are as follows:

<u>Fiscal year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 8,483,033	\$ 8,330,131	\$ 16,813,164
2008	8,308,033	8,071,382	16,379,415
2009	8,756,758	7,649,370	16,406,128
2010	8,890,003	5,910,544	14,800,547
2011	8,507,000	6,842,720	15,349,720
2012-2016	41,374,000	29,601,503	70,975,503
2017-2021	33,990,027	14,632,090	48,622,117
2022-2026	32,817,000	5,503,914	38,320,914
2027-2031	3,972,000	255,747	4,227,747
	<u>\$ 155,097,854</u>	<u>\$ 86,797,401</u>	<u>\$ 241,895,255</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Bonds

General obligation bonds payable as of June 30, 2006 are as follows:

<u>Series</u>	<u>Interest Rate</u>	<u>Payable Through</u>	<u>Original Issue</u>	<u>Balance July 2, 2006</u>
1984	5.00	2008	\$ 663,000	\$ 90,000
1986	5.00	2010	1,118,000	318,003
1987	6.13	2011	1,870,000	659,000
1987	5.00	2011	283,000	90,000
1989	5.00	2014	85,000	41,000
1991	5.00	2015	580,000	306,000
1992	3.26-6.41	2007	4,745,000	545,000
1994	5.00-7.71	2013	18,890,000	10,025,000
1996	4.70-6.58	2015	15,955,000	10,160,000
1994	5.63	2018	2,200,000	1,594,000
1996	4.50	2019	776,000	578,027

<u>Series</u>	<u>Interest Rate</u>	<u>Payable Through</u>	<u>Original Issue</u>	<u>Balance July 2, 2006</u>
1999	4.86-6.34	2106	\$ 13,300,000	\$ 9,520,000
2000	2.70-7.29	2024	3,150,000	2,765,000
2000	2.70-7.29	2026	10,350,000	8,780,000
2002	2.70-5.60	2026	9,845,000	9,005,000
2002	2.70-5.60	2026	125,000	100,000
2002	5.00-5.60	2026	1,360,000	1,230,000
2003	1.65-5.00	2028	9,900,000	9,245,000
2004	2.36-6.00	2029	1,575,000	1,485,000
2005	4.37-5.00	2024	1,610,000	1,510,000
2004	2.52-5.00	2029	370,000	360,000
2004	2.52-5.00	2029	460,000	440,000
2006	5.32-6.25	2021	9,910,000	9,510,000
2000	4.75	2030	500,000	489,000
2006	4.74-5.00	2025	11,015,000	10,700,000
2006	4.74-5.00	2025	11,020,000	10,705,000
1999	4.50	2030	1,640,000	1,603,000
			<u>\$133,295,000</u>	<u>\$101,853,030</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Federal loans and notes

Sec. 108 loan of \$8,000,000 payable in annual installments fluctuating from \$200,000 to \$600,000 at 7.50% interest rate until 2019, secured by building and adjacent parking facility owned by the Municipality and appraised at an aggregate fair market value of approximately \$11,750,000 .	\$ 6,600,000
Sec. 108 loan \$2,545,000, interest from 1.21% to 4.44% payable in annual installments from \$350,000 to \$500,000 until year 2009, secured by public facilities of the Municipality.	1,820,000
Sec. 108 loan \$1,400,000, interest at 6.57% payable in annual installments from \$125,000 to \$270,000, until year 2011, secured by public facilities of the Municipality.	<u>1,140,000</u>
Total federal loans and notes	<u>\$ 9,560,000</u>

Loans

Operational loan of \$2,065,000 payable in annual installments from \$35,000 to \$165,000 with interest fluctuating from 3.65 to 6.67% until 2027, secured by the Municipality.	\$ 1,915,000
Operational loan of \$2,350,000 payable in annual installments from \$270,000 to \$400,000 with interest of 5.5% until 2009, secured by the Municipality.	1,135,000
Operational loan of \$580,000 payable in annual installments from \$7,250 to \$29,000 at 8% interest until 2007, secured by the Municipality.	29,000

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Operational loan of \$540,662 payable in annual installments from \$6,758 to \$27,033 at 8% interest until 2008, secured by the Municipality.	60,824
Operational loan of \$5,185,000 payable in annual installments from \$90,000 to \$400,000 with interest fluctuating from 3.65 to 6.67 until 2027, secured by the Municipality.	4,795,000
Operational loan of \$305,000 payable in annual installments from \$95,000 to \$110,000 with interest fluctuating of 5.00 until 2007, secured by the Municipality.	110,000
Operational loan of \$640,000 payable in annual installments from \$80,000 to \$110,000 with interest fluctuating of 5.00 until 2011, secured by the Municipality.	475,000
Operational loan of \$15,385,000 payable in annual installments from \$260,000 to \$1,185,000 with interest fluctuating from 3.65 to 6.40 until 2027, secured by the Municipality.	14,235,000
Operational loan of \$1,385,000 payable in annual installments from \$245,000 to \$305,000 with interest fluctuating from 3.59 to 4.50 until 2010, secured by the Municipality.	1,140,000
Operational loan of \$10,015,000 payable in annual installments from \$300,000 to \$765,000 with interest fluctuating from 5.00 to 5.581 until 2025, secured by the Municipality.	9,715,000
Operational loan of \$10,075,000 payable in annual installments from \$255,000 to \$855,000 with interest fluctuating from 5.841 to 6.071 until 2026, secured by the Municipality.	<u>10,075,000</u>
Total loans	<u>\$ 43,684,824</u>
Total long-term debt governmental activities	<u>\$155,097,854</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Long-term debt for business-type activities at June 30, 2006 is summarized as follows:

Special bond obligation for \$500,000 to provide financing for the construction and rehabilitation of housing project for citizens of low and moderate income; annual interest rate at 2% with maturity on January 1, 2010, secured by the Municipality.	\$280,500
Special bond obligation for \$300,000 to provide for financing the reconstruction and rehabilitation of housing project for citizens of low and moderate income; annual interest rate at 2% with maturity on July 30, 2012, secured by the Municipality.	<u>209,371</u>
Total long-term debt for business-type activities	<u>\$489,871</u>

The debt service requirement for the long-term debt of Enterprise funds is scheduled as follow:

<u>Fiscal year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 96,320	\$ 10,393	\$ 106,713
2008	84,227	7,316	91,543
2009	104,010	5,636	109,646
2010	130,199	2,015	132,214
2011	35,269	1,320	36,589
2012-2013	39,846	647	40,493
	<u>\$ 489,871</u>	<u>\$ 27,327</u>	<u>\$ 517,198</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 8 - Retirement plans

Retirement System of the Commonwealth of Puerto Rico

The Municipality participates in the Employee's Retirement System of the Government of Puerto Rico and its instrumentalities (ERS), a multiple-employer contributory retirement plan, which covers only eligible full-time employees. The system provides retirement, death, and disability benefits and annuities to Commonwealth employees not covered by their own systems.

Commonwealth legislation required 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 participants' gross salary. Total employer contributions during the year ended June 30, 2006 amounted to approximately \$ 2,597,137.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1991, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employees participating 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 on or after January 1, 2000 will only be allowed to become members of the System 2000. System 2000 will reduce the retirement age from 65 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 the System 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% of the employees' salary up to a maximum of 10%) will be invested in account which 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 System 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.

For the year ended June 30, 2006, total covered payroll was approximately \$28 million. Covered payroll refers to all compensation paid by the Municipality to employees covered by the ERS on which contributions to the pension are based.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

The amount of the annuity shall be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation multiplied by the number of years of creditable service in excess of twenty years, for those employees covered after March 31, 1990, the annuity shall be equal to one and one-half percent of the average compensation multiplied by the number of years of creditable service, in no case shall the annuity be less than \$2,400.

Retirement plan of Head Start Program

Effective January 1, 2002, the Municipality created a retirement plan (the Plan) for all employees of the whose salaries were funded with the Head Start federal financial award and which have at least one year of service and are age twenty-one or older. The Plan is part of the Popular Master Defined Contribution Retirement. The Plan is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

The Municipality was required to contribute three percent (3%) of the employees' annual compensation. Participants may contribute based on after tax contributions amounts representing up to ten percent (10%) of the aggregate compensation paid to the employee, excluding the Christmas Bonus.

Participants are immediately vested in their contributions plus actual earnings thereon. Vesting is based on years of continuous service. The participant vesting schedule on such portion of their accounts is described below:

<u>Completed years of service</u>	<u>Vested percentage</u>
Less than 3 years	0%
At least 3 years	20%
At least 4 years	40%
At least 5 years	60%
At least 6 years	80%
At least 7 years	100%

The vesting provisions consider years of service before the employer established this Plan.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

On termination of service due to death, disability or retirement, a participant or beneficiary may elect to receive a lump-sum amount equal to the value of the participants' vested interest in his/her account, or maintain the funds in the Plan. Also, ten years annuities are allowed under the plan. The normal retirement age is the latter of the date a participant attains his 65th birthday or the fifth anniversary of the first day of the plan year in which he/she commenced participation in the Plan. Early retirement distributions are not permitted. Under the provisions of the Plan, participants are not permitted to withdraw any amount contributed by the employer from the plan, unless separated from employment.

During the year ended June 30, 2006, the Municipality contributions to this plan amounted to approximately \$233,000. At June 30, 2006, the Municipality had a restricted amount of \$938,502, which is also reported as part of the accrued liabilities in the Statement of Net Assets for the vested benefits to Plan's participants.

Note 9 - Commitments

Operating leases

The Municipality leases various properties and equipment under operating lease agreements, which generally have terms of one year or less and are automatically renewed if sufficient funds are available. Lease agreements covering periods in excess of one-year are cancelable at the Municipality's option upon 30 days written notice to the lessor. Rental expenditures for the year ended June 30, 2006 amounted to approximately \$1,541,493.

Future operating lease commitments are scheduled as follows:

2007	\$ 20,997
2008	<u>18,900</u>
	<u>\$ 39,897</u>

General construction of capital project commitments

The Municipality has commitments to invest approximately \$75,643,250 to complete construction and rehabilitation projects at several locations within the Municipality, which is allocated between Federal and Municipal funds for \$13,567,195 and \$62,076,055, respectively to satisfy these projects.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Solid waste disposal contract

In January 1984, the Municipality contracted E.C. Waste Inc. to provide the service of for the recollection, management and disposal of solid waste. This contract was amended in March 1994, September 2001, April and December 2003 to incorporate additional services related with those previously mentioned. In the contract it was established that the Municipality is committed to pay E.C. Waste Inc. \$10.50 per unit recollected applied to a starting minimum of 40,000 units with annual increases of two and a half percent (2.5%) up to fiscal year to be ended at June 30, 2010. Expenditure for the year ended June 30, 2005 for this service amounts to \$5,553,600. The scheduled payments for this commitment are disclosed as follows:

2007	\$ 5,688,000
2008	5,827,200
2009	5,971,200
2010	3,060,000
	<u>\$ 20,546,400</u>

In addition, the Municipality is committed to pay an additional \$34 per tons that the Municipality transports and deposits in the E.C. Waste, Inc.'s center of recollection of such solid wastes for their processing. The price of the rate is also subject to an annual increase of two and a half (2 ½ %). During the fiscal year ended June 30, 2006 the cost for the Municipality for this additional service amounted to approximately \$925,000.

Contributions to the operations of the Fine Arts Center

On August 9, 2002, the Autonomous Municipalities' Law was amended to allow the creation of non-profit private entities by municipal governments, universities, and the private sectors to carry out public purposes.

Under this authorization it was created "Corporación de Bellas Artes de Caguas" (COBAC) to carry out the activities that, until June 30, 2004, were being executed as an enterprise fund of the Municipality. On October 8, 2004, representatives of the Municipality and COBAC signed a 15-year lease contract, transferring to COBAC the operations of the Fine Arts Center (FAC) effective on July 1, 2004. As established in such lease contract, the Municipality will bill COBAC an annual rental fee of \$1,000.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

The Municipality is scheduled to make a 5-year annual contribution as part of the commitments that each representation of the Board (government, universities and the private sector) has to do, as established by Law. The contribution made by the Municipality to COBAC for the year ended June 30, 2006 was \$699,233. The remaining contributions are as follows:

2007	\$ 524,425
2008	349,617
2009	<u>174,800</u>
	<u>\$1,048,842</u>

On the other hand, the Municipality's representation in the COBAC's Board of Directors is four of a total of seventeen members, which constitutes twenty two percent of the voting power in the Board.

Note 10 - Contingencies

Litigation

The Municipality is a defendant in 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 \$4,081,762 in the government-wide statements for anticipated unfavorable judgments.

The amount presented in the general long-term debt of the statement of net assets represents the amount estimated as probable liability, which will require future available financial resources for its payment. The Municipality's administration and legal counsel believes that the ultimate liability in excess of amounts provided would not be significant. In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in the discovery stage. Certain of these claims are covered by insurance. Legal counsel with the information currently available cannot determine the final outcome of these claims. As a result, the accompanying general-purpose financial statements do not include adjustments, if any, that could result from the resolution of these legal proceedings.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Federal financial assistance

The Municipality receives financial assistance from the federal government in the form of grants or entitlements. The Municipality recognizes federal grant revenues when the related grant agreements are approved and notified by the federal agencies by written communication. All grants are subject to financial and compliance audits by the grantor agencies, which could result in requests for reimbursement by the grantor agencies for expenditures, if disallowed under the terms of the grants. These amounts, if any, of expenditures, which may be disallowed by the granting agencies, cannot be determined at this time. The Municipality's administration believes that such disallowances, if any, will not have a material adverse effect on the financial position of the Municipality.

Note 11 - Healthcare costs

During the year ended June 30, 2000 the Governor of the Commonwealth of Puerto Rico required to the municipalities of Puerto Rico an annual contribution to subsidy the cost of the implementation and administration of the Healthcare Reform. Such contributions are required to be disbursed from general fund operating budget. Total contributions made by the Municipality amounted to approximately 5,819,333 for the fiscal year ended June 30, 2006.

Note 12 - Accrued liabilities

At June 30, the Municipality had the following accrued liabilities:

	<u>Balance at</u> <u>June 30, 2005</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at</u> <u>June 30, 2006</u>	<u>Due within</u> <u>one year</u>
Accrued compensated absences	\$ 8,464,686	\$ 1,312,637	\$ (1,105,215)	\$ 8,672,108	\$ 987,000
Accrued legal claims	1,762,664	2,463,714	(144,616)	4,081,762	1,762,664
	<u>\$ 10,227,350</u>	<u>\$ 3,776,351</u>	<u>\$ (1,249,831)</u>	<u>\$ 12,753,870</u>	<u>\$ 2,749,664</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 13 - Subsequent events

Municipal Citizen's Contribution

On July 4, 2006, the Governor of Puerto Rico signed Act No. 117, known as the "Tax Fairness Act of 2006" (hereinafter the "Act"). Among its provisions, the Act provides for a sales and use tax of 5.5% at a Commonwealth level and authorizes the municipalities to impose a sales and use tax of 1.5% at the municipal level. On July 12, 2006, our Mayor signed Ordinance No. 06A-6, Series 2006-2007, which imposes the 1.5% sales and use tax authorized by the Act, effective on September 1, 2006. Consequently, the Ordinance 05A-46, as amended, was rescinded effective on August 31, 2006.

Sales tax collections from July 1 to October 31, 2006 amounted to \$4 million. The Municipality projects collections of more than \$16 millions for fiscal year 2006-2007.

General Obligation Bonds and Special Operational Loan

On July 11, 2006 the Municipality's Legislature approved the issuance of \$8,060,00 Serial A general obligation bonds, through the Ordinance No. 06A-4 2006-2007, at an interest rate of 0.16% over the LIBOR rate with maturity at July 1, 2031. The financing agreement was formalized with a private local bank.

On August 17, 2006, the Governmental Development Bank for Puerto Rico approved and disbursed on behalf of the Municipality proceeds for a \$8, 575,000 operational loan. The financing was initially approved by the Municipality's Legislature through the Ordinance 06-A serial 2006-2007.

The proceeds resulting from these financing agreements will be used for various capital projects in benefits of the citizens of Caguas.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Note 14 -Prior period adjustments

Governmental fund statements

The beginning fund balances of total governmental funds at July 1, 2005 have been restated by to account due to the corrections in the following non-exchange transactions:

Description	General	Housing and Rental	Public Residential	Head Start and Youth	Capital Project	Other Governmental	Total
(Understatement) of deferred revenue at June 30, 2005	\$ (5,543,642)	\$ -	\$ -	\$ -	\$ 9,985,118	\$ 1,694,091	\$ 6,135,567
(Overstatement) of due from federal agency at June 30, 2005	-	(3,184,899)	(1,005,683)	(3,480,175)	(9,985,118)	(2,530,480)	(20,186,355)
Over (understatement) in 2004-2005 expenditures	-	10,724,465		(1,815,220)		6,457,778	15,367,023
(Under) overstatement if expenditures in years previous to 2004-2005	-	(10,724,465)	484,054				(10,240,411)
(Under) overstatement of accounts payable at June 30, 2005	-	-	40,502		(5,145,043)		(5,104,541)
(Over) understatement in federal grants of year 2004-05	-	-	(186,654)	(861,706)	(23,406,969)	(2,410,209)	(26,865,538)
Under (overstatement) of federal grants previous to year 2004-05	-	-	(297,700)	2,899,238	16,390,671	(3,177,398)	15,814,811
	<u>\$ (5,543,642)</u>	<u>\$ (3,184,899)</u>	<u>\$ (965,481)</u>	<u>\$ (3,257,863)</u>	<u>\$ (12,161,341)</u>	<u>\$ 33,782</u>	<u>\$ (25,079,444)</u>

Government wide statements

The beginning net assets of governmental activities at July 1, 2005 have been restated due to the corrections in the following non-exchange transactions:

Retroactive recognition of infrastructure capital assets	\$ 132,852,696
Retroactive recognition of accumulated depreciation in major capital assets	(23,749,829)
Overstatement of revenues in Public Housing Administration project	(186,654)
Overstatement of revenues in Section 8 and Home programs	(161,587)
Overstatement of revenues in Head Start, Child Care and Child Care Food programs	(3,955,402)
Overstatement of revenues in other operating federal grants	(1,687,458)
Retroactive treatment of impairment loss in Turabo Recreational Park capital asset	(4,935,501)
Understatement of deferred volume of business tax revenue	(19,663,584)
Overstatement in capital grants in prior years	(17,250,554)
Overstatement in expenses of housing activities	10,937,253
Overstatement in expenses of public safety activities	6,457,778
	<u>\$ 78,657,158</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAGUAS

Notes to Financial Statements (continued)
June 30, 2006

Business-type activities

The beginning net assets of business type activities at July 1, 2005 have been restated by \$1,550,578 to correct understatement of capital grants in the Multi-tenant activity.



Accountants &
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MUNICIPALITY OF CAGUAS

SINGLE AUDIT PACKAGE
Fiscal Year Ended
June 30, 2006

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TABLE OF CONTENTS

Page

AUDITORS' SECTION

INDEPENDENT AUDITORS' 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	1
INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133.....	3
SCHEDULE OF FINDINGS AND QUESTIONED COSTS.....	6
REPORT ON THE STATUS OF UNCORRECTED MATERIAL FINDINGS AND RECOMMENDATIONS FROM PRIOR AUDITS THAT AFFECT THE FINANCIAL STATEMENT AUDITS AS REQUIRED BY GOVERNMENT AUDITING STANDARDS.....	11

AUDITEE'S SECTION

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS AS REQUIRED BY OMB CIRCULAR A-133	12
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS.....	13
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS.....	14
VIEWS OF RESPONSIBLE OFFICIALS AND PLANNED CORRECTIVE ACTIONS.....	15



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INDEPENDENT AUDITORS' 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

Hon. William Miranda Marín, Mayor
Commonwealth of Puerto Rico
Municipality of Caguas

We have audited the basic financial statements of the Municipality of Caguas (The Municipality) as of and for the year ended June 30, 2006 and have issued our report thereon dated December 15, 2006. 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's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment could adversely affect the Municipality's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and responses as item 2006-1.



Accountants &
business advisers

Hon. William Miranda Marín, Mayor
Commonwealth of Puerto Rico
Municipality of Caguas
Page 2

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions, and accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described above to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain 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*.

This report is intended solely for the information and use of the Mayor, the Municipal Assembly, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



December 15, 2006

PKF, LLP
License No. 22
Expires on December 1, 2007

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

Hon. William Miranda Marín, Mayor
Commonwealth of Puerto Rico
Municipality of Caguas

Compliance

We have audited the compliance of the Municipality of Caguas (The Municipality) 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, 2006. The Municipality's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on the Municipality'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 of America; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Municipality's compliance with those requirements and performing such other procedures, as 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 on the Municipality's compliance with those requirements.

Hon. William Miranda Marín, Mayor
Commonwealth of Puerto Rico
Municipality of Caguas
Page 2

In our opinion, the Municipality of Caguas 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, 2006.

Internal control over compliance

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

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Hon. William Miranda Marín, Mayor
Commonwealth of Puerto Rico
Municipality of Caguas
Page 3

Schedule of Expenditure of Federal Awards

We have audited the financial statements of the governmental activities, the business type activities, each major fund, and the aggregate remaining fund information of Municipality of Caguas (Municipality) as of and for the year ended June 30, 2006, and have issued our report thereon dated December 15, 2006. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise Municipality's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 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.

This report is intended solely for the information and use of the Mayor, the Municipal Assembly, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



PKF, LLP
License No. 22
Expires on December 1, 2007

March 15, 2007

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For the Fiscal Year Ended June 30, 2006

SECTION 1 – SUMMARY OF AUDITOR'S RESULTS

Financial Statements:

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

1. Material weakness identified? Yes

2. Reportable condition(s) identified that are not considered to be material weakness? No

Noncompliance material to financial statements noted? No

Federal awards:

Internal control over major programs:

1. Material weakness(es) identified? No

2. Reportable condition(s) that are not considered to be material weaknesses? No

Type of auditor's report issued on compliance for major program? Unqualified

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510 (a)? No

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Cluster

14.218	Community Development Block Grant Entitlement
93.600	Head Start Administration for Youth and Children
14.239	Home Investment Partnership Program
14.871	Section 8 Housing Choice Voucher
14.850	Public and Indian Housing (passed-through the Puerto Rico Public Housing Administration)
93.914	HIV Emergency Relief
10.588	USDA Child and Adult Care Food Program (passed-through the Department of Education of the Commonwealth of Puerto Rico)

Dollar threshold used to distinguish between Type A and Type B programs: \$969,194

Auditee qualified as a low-risk auditee? No

SECTION 2 – FINANCIAL STATEMENT FINDINGS

Finding No. 2006-1

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Internal Control Structure Design Material Weakness
Questioned Cost:	None

Condition:

We noted the following internal control situations in the use of the SAP Accounting System.

1. The subsidiary of capital assets was not properly updated, specially the construction in progress and infrastructure capital assets.
2. The balances of certain federal grants receivable that operate as expenditure driven grants did not have activity during the year 2005-2006.

Criteria:

The Puerto Rico Municipalities' Law establishes the following:

1. The administrative units have within their duties the establishment and maintenance of internal controls that allow for the verification of quantitative and qualitative compliance of programs, projects and activities of the Municipality [Article 6.003 (d)].
2. The Director of Finance should supervise the internal controls and tasks related with the fund accounting, transactions and other related financial matters [Article 6.005 (c)].
3. The Municipalities should maintain systems and procedures oriented to improve the internal controls This include internal control procedures regarding federal grant receivables and capital assets.

Cause:

1. The Municipality's Finance Department has not received and does not have in the SAP System the related data obtained by the consulting firm in charge of performing the update of the accounting of construction in progress account.

2. No reconciliation procedures have been performed between the data of capital assets maintained in the SAP System by the Municipality's Department of Finance with the capital assets' subsidiary prepared by the external consulting firm.
3. The transactions that affect the federal grants receivable are not accounted in SAP System. Also, the Departments in the Municipality which are in charge of making the requests of funds to the Federal agencies should maintain well informed the Accounting Area of the Municipality's Finance Department of the requests pending to be received by the Federal agencies.

Effect:

These situations caused the proposal of audit adjustments in order to establish reasonable balances for capital assets and federal grant receivables.

Recommendations:

Capital assets:

The Finance Director should request to the external consulting firm in charge of gathering information about construction projects and depreciable real property to provide reports of the construction projects finished. The balances of such projects should be supported by the corresponding evidence.

In addition, the Finance Director should request to the external consulting firm the inventory of capital assets at June 30, 2006 in order to update the inventory of capital assets maintained in the Finance Department.

Federal grant receivables:

Expenditure driven grants occur in two situations. The first situation occurs when the Municipality made the disbursement with resources of general fund and then claims reimbursement to the Federal grantor by the amounts already disbursed, showing evidence of their occurrence. A receivable should be recognized by amounts claimed for reimbursement to the Federal agencies that at June 30 have not been received by the Municipality.

In the second situation the Municipality receives the services from vendors, contractors and employees and by this way incurs in the allowable expenditure or cost. Then the employees in charge of requesting funds to the corresponding Federal agencies list the corresponding invoices, certifications and/or payrolls and prepare a request of draw-downs to the Federal agencies. Such requests should detail evidence of such costs incurred but not paid for demonstrating to the Federal grantor that the requests are made to satisfy immediate disbursement needs. At this time the Municipality should recognize an account receivable and at June 30, the amount of federal grants receivable should consist of those requests for draw-downs submitted by the Municipality and pending of disbursement by the Federal agencies. Such receivables are reduced based on the draw-downs received by the Municipality.

Based on the situations described above, we recommend to the Finance Director the maintenance of a subsidiary of federal grants receivable based in the listings of outstanding requests for reimbursements or draw-downs, as applicable for individual Federal award in order to facilitate the accounting of federal grants receivable in SAP.

END FINDING NO. 2006-1

SECTION 3 – FEDERAL AWARD FINDINGS

None.

REPORT ON THE STATUS OF UNCORRECTED MATERIAL FINDINGS AND RECOMMENDATIONS FROM PRIOR AUDITS THAT AFFECT THE FINANCIAL STATEMENT AUDITS AS REQUIRED BY GOVERNMENT AUDITING STANDARDS

Finding No. 2005-1

Audit Finding Description:

We noted the following internal control weaknesses in the use of the SAP Accounting System.

- The balances per general ledger control accounts for encumbrances do not tie with their corresponding subsidiaries.*
- The subsidiary of capital assets acquisition was not properly updated. In addition, the general ledger control account of construction in progress is not properly updated with transactions related with the construction projects.*
- The salary expenditures accounted in the Appropriations, Encumbrances, Expenditures and Fund Balance Reports of all funds were not in agreement with amount of salaries reported in the FICA tax returns.*
- The balances of inter-fund loans (due from/to other funds) are not periodically updated and reconciled with their related general ledger control accounts.*
- The effect of the amortization of principal and interest expense on enterprise fund notes payable is not recorded in the accounting of Community Development Bank fund.*

Audit finding status:

The situations regarding the encumbrances, inter-fund loans, salaries and notes payable of the Community Development Bank were fully corrected. The situation of capital assets was partially corrected and corrective actions are still recommended due to situation mentioned in Audit Finding 2006-1.

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS AS REQUIRED BY OMB CIRCULAR A-133

Finding No. 2005-2

Audit Finding Description:

During our audit of the Head Start Program's participant files, we found: two (2) Head Start participants' files of a sample of twenty-four (24) that did not include allowable evidence of family income as required by federal regulations. Files included a certification signed by the parent(s)/guardian(s) stating the family income. According to said certifications, the participants' family incomes were below the HHS 2004 and 2005 Poverty Guidelines.

Audit finding status:

On January 27, 2006 the Director of the Head Start Program addressed a memorandum to the designated personnel providing the instructions of all necessary evidence to be required to each participant's family. Also, during our test performed during current year audit over the Head Start participants' file we noted that all participants files tested contained all necessary evidence of family income.

We consider that condition was corrected.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FISCAL YEAR ENDED JUNE 30, 2006

<u>Federal Grantor</u>	<u>Program Title</u>	<u>Federal CFDA Number</u>	<u>Grant Number</u>	<u>Expenditures</u>
US Department of Agriculture	Child and Adult Care Food Program (Pass-through the Department of Education of the Commonwealth of Puerto Rico)	10.558	N/A	\$ 1,005,011
US Department of Health and Human Services	Head Start Program	93.600	02CH0263/20	12,945,159
	HIV Emergency Relief Project Grant	93.914	H89HA00037-10-1	2,078,054
	Child Care and Development Block Grant (SENDEC)	93.575	N/A	507,554
	Self Help Housing	N/A		180,505
	Geriatric Elderly Care Program (Pass through the Department of the Family of the Commonwealth of Puerto Rico)	93.044	N/A	135,346
	Integrated Health for the Prevention and Attention against the Abuse to the Women (Pass-through the Office for the Procurement of the Woman of the Commonwealth of Puerto Rico)	N/A	N/A	29,794
US Department of Housing and Urban Development	Public and Indian Housing (Pass-through the PR Department of Housing for the Administration of Public Housing)	14.850	03-1978	873,524
	Community Development Block Grant /Entitlement Grants	14.218	B-01-MC-72-0001	4,418,506
	Emergency Shelter Grants Program	14.231	S-01-MC-72-0005	195,292
	HOME Investment Partnerships Program	14.239	M-01-MC-72-0203	2,324,971
	Section 8 Housing Choice Vouchers	14.871	RQ-007-V0	6,039,152
Federal Transportation Administration (FTA)	Grant for the Acquisition of Trolleys	20.507	N/A	76,944
US Department of Justice	Byrne Formula Grant Program ("Pass-through the Department of Justice of the Commonwealth of Puerto Rico)	16.579	N/A	108,277
	Weed and Seed	16.595	2002-WS-QX-0131	115,804
Federal Emergency Management Agency	Disaster Assistance (Pass-through the Office of the Governor of the Commonwealth of Puerto Rico)	83.516	N/A	241,351
US Department of Commerce - Economic Development Administration (EDA)	Multi-tenant Project	N/A	01-11-02519	653,223
	Loans program for Economic Development	N/A	N/A	90,000
US Department of Homeland Security	Homeiand Security Grant Program	97.067	N/A	287,996
Total Expenditures				\$32,306,463

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Fiscal Year Ended June 30, 2006

NOTE 1 - GENERAL

The accompanying schedule of expenditures of federal awards presents the expenditures, for the fiscal year ended June 30, 2006, of all the federal assisted programs of the Municipality of Caguas.

NOTE 2 - ACCOUNTING BASIS

The schedule was prepared following the modified accrual basis of accounting, which is further explained in Note 1 of the basic financial statements of the Municipality of Caguas for the fiscal year ended June 30, 2006.

NOTE 3 - SUBRECIPIENTS

During fiscal year 2005-06, the Municipality disbursed \$1,820,422 to sub-recipients for the realization of healthcare, public service, and community development projects. The following entities received sub-awards from the Municipality's federal financial assistance programs:

Federal Program	Sub-recipient Entities	2005-2006 Disbursements
HIV Emergency Relief Project Grants	*Centro Clínico Nuevas Actitudes*	68,806
	Asociación Familiares y Amigos Pacientes SIDA	126,914
	Fundación de Desarrollo Comunal (FUNDESCO)	17,552
	Voluntarios y Acompañantes con el SIDA	18,157
	Gurabo Community Health Center	609,920
	Hogar CREA	587,345
	Asociación Puertorriqueña de Servicios y Ayuda al Paciente con SIDA (APSAPS)	140,664
	Iniciativa Comunitaria de Investigación	13,708
Subtotal		\$1,582,866
Emergency Shelter Grant	<i>Casa San Gerardo, Inc.</i>	10,360
	<i>*Instituto de Orientación y Terapia Familiar* (INOTEF)</i>	30,919
	Centro Clínico Nuevas Actitudes	45,334
	<i>*Hogar Resurrección*</i>	29,389
	Fundación de Desarrollo Comunal (FUNDESCO)	30,505
	Corp. Milagros de Amor	60,044
Subtotal		206,551
Community Development Block Grant Entitlement Grants	<i>*Instituto de Orientación y Terapia Familiar* (INOTEF)</i>	31,005
Total		\$ 1,820,422

VIEWS OF RESPONSIBLE

OFFICIALS AND PLANNED CORRECTIVE ACTIONS

SEE APPENDIX



Lcdo. William Miranda Marin
Alcalde

March 26, 2007

To whom may concern:

CORRECTIVE ACTION PLAN

Contact person: Mr. Víctor M. Coriano Reyes, Director of Finance

I have provided the following instructions:

Capital assets:

We will request to the external consulting firm in charge of gathering information about construction projects and depreciable real property to provide its reports and files of the construction projects finished. The balances of such projects should be supported by the corresponding evidence.

Also, We will request to the external consulting firm the inventory of capital assets at June 30, 2006 and 2005 in order to update the inventory of capital assets maintained in the Finance Department.

In addition, and to maintain the corrective action, We will request to the consulting firm to submit quarterly reports of the construction projects terminated. Such reports should contain at a minimum the following:

- Project name
- Physical location
- Cost incurred

Page2

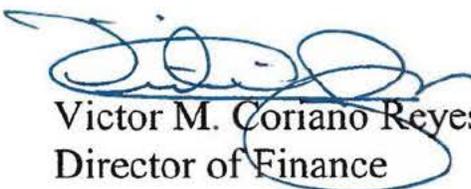
Corrective Action Plan

- Source of funding
- Contractor's name
- Projects' termination date

Finally we will request that in the documents the consulting firm consider that the amounts included in the finished construction projects be in agreement with the amounts established in the contracts formalized and directly related with the projects, including their amendments (e.g. construction, architects and engineers).

Federal grant receivables:

Considering that we have various grants that work under a expenditure driven basis, We will provide instructions to the personnel of the Accounting Area to design a subsidiary of federal grants receivable based in the listings of outstanding requests for reimbursements or draw-downs, as applicable for individual Federal award in order to facilitate the accounting of federal grants receivable in SAP. To help in the implementation of this recommendation we will coordinate with the Accountants and other employees that work with such grants, specially in its accounting and request for draw-downs and/or reimbursement, to provide to the Finance Department information of such requests, specially those outstanding at year-end.



Victor M. Coriano Reyes
Director of Finance



Lcdo. William Miranda Marin
Alcalde

26 de marzo de 2007

Sra. Ana L. Vélez Martínez
Directora Auxiliar
Departamento de Finanzas
Municipio Autónomo de Caguas

Estimada señora Vélez Martínez:

Recientemente recibimos el borrador del Informe de la Auditoría Sencilla que se realizó en nuestro Municipio para el año que terminó el 30 de junio de 2006. En dicho documento se incluyó la siguiente recomendación relacionada con los Programas Federales que requieren acción correctiva de parte del Departamento de Finanzas:

- Mantener un Subsidiario de las Cuentas por cobrar a los Programas Federales basado en el listado de recobros o peticiones de fondos pendientes, según aplique a cada programa federal. Esto con el propósito de facilitar la contabilidad de las Cuentas por cobrar de los Programas Federales en el Sistema de SAP.

Como es de su conocimiento, los desembolsos de estos Programas Federales se emiten de la Cuenta General del Municipio y luego se recobran de los distintos programas. El no llevar un registro de las distintas peticiones de fondos ha ocasionado que no se mantengan balances actualizados de las peticiones pendientes de recibirse al 30 de junio.

Sra. Ana L. Vélez Martínez

26 de marzo de 2007

Página 2 de 2

Para subsanar esta situación es imprescindible mantener un Subsidiario de las Cuentas por Cobrar a los Programas Federales basado en las peticiones pendientes de recibirse de cada programa. Además, es imprescindible que cada vez que se genere una petición de fondos, el Departamento responsable someta copia de la petición al Departamento de Finanzas, División de Contabilidad. Esto permitirá mantener balances correctos de estas cuentas por cobrar en nuestro Sistema de Contabilidad.

Cuento con su colaboración para corregir estas deficiencias a la brevedad posible.

Cordialmente,



Victor M. Coriano Reyes
Director de Finanzas