

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL
AREA DE ARCHIVO DIGITAL

MUNICIPIO DE CAMUY
AUDITORIA 2003-2004
30 DE JUNIO DE 2004

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY**

**BASIC FINANCIAL STATEMENTS AND
SUPPLEMENTAL SCHEDULE**

With Independent Auditors' Report Thereon
June 30, 2004

Conf No. 5-258

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
Basic Financial Statements and
Supplemental Schedule
June 30, 2004**

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INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Camuy of the Commonwealth of Puerto Rico (the "Municipality"), as of and for the year ended June 30, 2004, which collectively comprise the Municipality's basic financial statements as listed in the accompanying 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statement. 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 and the report of other auditors provide a reasonable basis for our opinion.

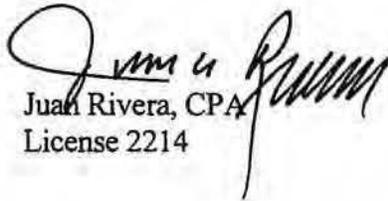
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Camuy of the Commonwealth of Puerto Rico as of June 30, 2004, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, on July 1, 2003 the Municipality has implemented a new financial reporting model, required for state and local governments established by the Governmental Accounting Standards Board ("GASB") Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis- for States and Local Governments. As more fully described in Note 1, as part of the adoption of the new financial reporting model, on July 01, 2003 the Municipality also adopted the provisions of

other pronouncements issued by GASB, the Accounting Principles Board ("APB") and the Financial Accounting Standards Board ("FASB).

The effects of implementing the aforementioned pronouncements have been reported as changes in accounting principles in the accompanying basic financial statements. Accordingly, the effects of such transactions have been retroactively reported as restatements of fund balances in the accompanying fund financial statements at July 1, 2003

The accompanying Management's Discussion and Analysis and the Budgetary Comparison Schedule-are not a required parts of the basic financial statements referred to above, but are supplementary information required by the Governmental Accounting Standards Board (GASB). 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 there on.


Juan Rivera, CPA
License 2214



December 16, 2004
Toa Baja, Puerto Rico

Stamp No. 2010603 of the Puerto Rico Society of Certified Public Accountants was affixed to the record copy of this report.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Management of the Municipality of Camuy of the Commonwealth of Puerto Rico (the Municipality) provides this *Management's Discussion and Analysis* (MD&A) for the readers of the Municipality's basic financial statements. This narrative represents an overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2004. Because this MD&A is designed to focus on the current year activities, resulting changes and currently known facts, we encourage readers to consider the information presented in this MD&A in conjunction with the additional information furnished in the accompanying basic financial statements.

During fiscal year ended June 30, 2004, the Municipality implemented the new required financial reporting standards established by Statement No. 34, *Basic Financial Statements – and Management's Discussion – and Analysis – for State and Local Governments*, issued by the Governmental Accounting Standards Board (GASB No. 34). According to this statement, significant required changes in content and structure have been made in the basic financial statements as of and for the fiscal years ended June 30, 2004 and 2003, which make them not easily comparable with prior years' financial statements. However, in future years, comparative analysis will be more meaningful and will go further in explaining the Municipality's financial position and results of operations.

FINANCIAL HIGHLIGHTS

a) Government-Wide Highlights

- **Assets** – The Municipality has reported assets amounting to \$24.6 million in the accompanying statement of net assets, of which the most significant are capital assets, cash, and tax receivables amounting to \$18.6 million, \$1.1 million, and \$2.4 million, respectively.
- **Liabilities** – The Municipality has reported liabilities amounting to \$12.1 million in the accompanying statement of net assets, of which the most significant are bonds and notes payable, deferred revenues, compensated absences, and accounts payable amounting to \$3.2 million, \$0.7 million, \$1.3 million and \$3 million respectively.
- **Net assets** – The assets of the Municipality exceeded its liabilities by \$12.5 million at June 30, 2004, which is presented as “net assets” in the accompanying statement of net assets. Restricted net assets and unrestricted deficit amounted to \$2.1 million and \$5.0 million, respectively. Net assets invested in capital assets amounted to \$11.1 million.
- **Net change in net assets** – The Municipality's net assets increased by \$.5 million during fiscal year ended June 30, 2004. Net assets at June 30, 2003 (as restated) amounted to \$12 million. The increase in net assets represents a positive result of operations and an improvement in the Municipality's overall financial position in comparison with the prior fiscal year.
- **Revenues** – The Municipality has reported total revenues amounting to \$12.2 million in the accompanying statement of activities, of which the most significant are tax revenues,

intergovernmental grants and contributions and taxes amounting to \$4.0 million and \$7.2 million, respectively.

- *Expenses* – The Municipality has reported total expenses amounting to \$11.7 million in the accompanying statement of activities.

b) Governmental Funds Highlights

- *Assets* – The Municipality's governmental funds have reported combined assets amounting to \$9.9 million in the accompanying balance sheet – governmental funds, of which the most significant are cash, due from other funds, taxes receivable and grants and contributions amounting to \$0.6 million, \$3.9 million, \$2 million and \$1.7 million, respectively.
- *Liabilities* – The Municipality's governmental funds have reported combined liabilities amounting to \$9.3 million in the accompanying balance sheet – governmental funds, of which the most significant are deferred revenues, due to other funds and due to governmental entities amounting to \$3.3 million, \$3.9 million and \$1.1 million respectively.
- *Governmental fund balances* – The Municipality's governmental funds reported combined fund balances amounting to \$0.5 million, of which \$4.2 million and \$-3.6 million represent reserved and unreserved fund balances, respectively.
- *Net change in governmental fund balances* – The Municipality's governmental fund balances increased by \$1 million during fiscal year ended June 30, 2004. Governmental fund balances at June 30, 2003, as restated, amounted to \$-0.4 million. The increase in net assets represents the excess of expenditures and other financing uses over revenues and other financing sources.
- *Revenues* – The Municipality's governmental funds have reported combined revenues amounting to \$11.2 million in the accompanying statement of revenues, expenditures and changes in fund balances – governmental funds, of which the most significant are intergovernmental grants and contributions, property taxes and municipal license taxes amounting to \$3.9 million, \$6 million and \$0.5 million, respectively.
- *Expenditures* – The Municipality's governmental funds have reported combined expenditures amounting to \$10.7 million in the accompanying statement of revenues, expenditures and changes in fund balances – governmental funds, of which the most significant are categorized as; general government; public housing and welfare; health and sanitation; urban and economic development and public safety amounting to \$4.1 million, \$1.7 million, \$1.5 million, \$1.6 million, and \$0.5 million respectively.

USING THIS ANNUAL REPORT

This annual report consist of a series of new financial statements with a change in the focus from the previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The Municipality's financial statements include three components: (1) the government-wide financial statements, (2) the fund financial statements, and (3) the notes to the financial statements (collectively known as the basic financial statements). This report also contains additional required supplementary information (budgetary schedules) and other supplementary information (combining financial statements) in addition to the basic financial statements themselves. These components are described below:

Government-Wide Financial Statements

The *government-wide financial statements* are designed to provide readers with a broad overview of the Municipality's operations and finance as a whole in a manner similar to private-sector business. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at the end of the fiscal year. These financial statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means that these financial statements follow methods that are similar to those used by most businesses. They take into account all revenues and expenses connected with the fiscal year ended June 30, 2004 even if cash involved have not been received or paid. The government-wide financial statements include the Statements of Net Assets and the Statement of Activities.

Statement of Net Assets

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

Statement of Activities

The statement of activities presents information showing how the Municipality's net assets changed during the fiscal year ended June 30, 2004. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenues for each function of the Municipality.

Both of the abovementioned financial statements present all the governmental activities of the Municipality, which consist mostly by taxes and intergovernmental revenues (such as federal grants). Most services provided by the Municipality fall into this category, including culture and education, general government, health and sanitation, public safety, public housing and welfare, etc.

Fund Financial Statements

The Municipality's fund financial statements, which consist of: (1) the Balance Sheet – Governmental Funds and (2) the Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds. These financial statements report the financial position and results of operations of the Municipality's governmental funds.

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

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

Governmental funds are used to account for all of the services provided by the Municipality. Governmental funds are used to account for essentially the same functions reported as governmental activities in the governmental-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources. They also focus on the balances of spendable resources available at the end of the fiscal year (June 30, 2004). This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Municipality's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Municipality, that is, evaluating the Municipality's near-term financing requirements.

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

For financial reporting purposes the Municipality has two major funds: (1) the general fund and (2) the joint resolution fund.

Notes to the Basic Financial Statements

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

Required Supplementary Information

The basic financial statements are followed by a section of required supplementary information consisting of a budgetary comparison between actual operating results with the original budget and the final amended budget for the general fund.

INFRASTRUCTURE ASSETS

Historically, a government's largest group of assets (infrastructure – streets, roads, bridges, etc.) have not been reported nor depreciated in governmental financial statements. GASB 34 requires that these assets be valued and reported within the governmental column of the Government-Wide Financial Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (modified approach) which periodically (at least every third year), by category, measures and demonstrates its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time.

As of July 1, 2002, the Municipality retroactively recorded the historical costs of infrastructure assets. Also the Municipality elected to depreciate infrastructure assets instead of using the modified approach.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of the Municipality's financial position. In the case of the Municipality, net assets (excess of assets over liabilities) amounted to \$12.5 million at June 30, 2004, compared to \$12 million at the end of the previous year, as restated.

The largest portion of the Municipality's net assets are invested in capital assets net of their related debt \$13.5 million. The Municipality's net assets is also composed of net assets amounting to \$12.5 million that are restricted for (1) future debt service payments, (2) the future acquisition or construction of capital assets and (3) other purposes, mainly the financing of federal and state assisted programs. In addition, the Municipality's net asset are reported net of an unrestricted deficit of \$3.5 million.

The unrestricted deficit is the consequence of previous budgets which did not provide funding for incurred long-term obligations such as compensated absences and others. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation. Consequently, the Municipality cannot draw from its existing assets to provide services to its citizens and depends on its taxing ability to continue its operations.

The portion of the Municipality's net assets invested in capital assets such as land, buildings, equipment, etc., less any outstanding related debt used to acquire those assets, are used by the Municipality to provide services to its citizens; consequently these assets are not available for future spending. Although the Municipality's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from the debt service fund, since the capital assets themselves cannot be used to liquidate these liabilities.

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

Current assets	\$ 6,027,454
Noncurrent assets	<u>18,611,781</u>
Total assets	<u>24,639,235</u>
Current liabilities outstanding	6,949,122
Noncurrent liabilities outstanding	<u>5,165,937</u>
Total liabilities	<u>12,115,059</u>
Net assets/(liabilities):	
Invested in capital assets, net of related debt	13,595,377
Restricted	3,983,740
Unrestricted	<u>(3,574,622)</u>
Total net assets	<u>\$ 12,524,176</u>

Changes in Net Assets

The Municipality's net assets increased by \$0.5 million. Approximately 24 percent of the Municipality's total revenues came from taxes, while 59 percent resulted from restricted and unrestricted capital and operating grants, contributions and reimbursements, including federal financial assistance. The Municipality's expenses cover a range of services. The largest expenses were for general government (39 percent), public housing and welfare (19 percent) and health and sanitation (14 percent).

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

Condensed Statement of Activities:

Revenues:	
Program revenues:	
Operating grants and contributions	\$ 1,826,291
Capital grants and contributions	470,288
Charges for services	36,190
General revenues:	
Property taxes	6,467,096
Municipal license taxes	502,804
Construction excise taxes	255,119
Unrestricted intergovernmental contributions and reimbursements	1,763,369
Unrestricted interest on deposits	4,579
Miscellaneous	379,484
Special items - Puerto Rico Electric Power Authority	<u>506,343</u>
Total revenues	<u>12,211,563</u>
Expenses:	
General government	4,651,986
Urban and economic development	2,240,922
Public safety	622,129
Health and sanitation	1,603,564
Culture, recreation and education	647,232
Public housing and welfare	1,760,033
Interest on bonds, notes and capital lease obligations	<u>181,324</u>
Total expenses	<u>11,707,190</u>
Net increase in net assets	504,373
Net assets - at beginning of year, as restated	<u>12,019,803</u>
Net assets - at end of year	<u>\$ 12,524,176</u>

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S GOVERNMENTAL FUNDS

As discussed 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 balance of *spendable resources*. Such information is useful in assessing the Municipality's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of fiscal year. The following is a condensed presentation of the Municipality's balance sheet and results of operations of governmental funds:

Condensed Balance Sheet - Governmental funds:

Total assets - major funds	\$ 7,927,599
Total assets - nonmajor funds	<u>1,989,646</u>
Total assets	<u>9,917,245</u>
Total liabilities - major funds	7,759,301
Total liabilities - nonmajor funds	<u>1,564,265</u>
Total liabilities	<u>9,323,566</u>
Fund Balances:	
Reserved - major funds	3,836,908
Reserved - nonmajor funds	425,381
Unreserved - major funds	<u>(3,668,610)</u>
Total net assets	<u>\$ 593,679</u>

Condensed Statement of Operations - Governmental funds:

Total revenues - major funds	\$ 8,381,035
Total revenues - nonmajor funds	<u>2,867,002</u>
Total revenues	<u>11,248,037</u>
Total expenditures - major funds	8,004,561
Total expenditures - nonmajor	<u>2,721,626</u>
Total expenditures	<u>10,726,187</u>
Other financing sources - major funds (excluding operating transfers among funds)	<u>-</u>
Special items, net	<u>506,342</u>
Net change in fund balances	<u>\$ 1,028,194</u>

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The accompanying statement of net assets reported total gross capital assets, at cost, amounting to \$31,370,798, of which \$13,286,415 represents infrastructure assets at June 30, 2004. The related accumulated depreciation and amortization of capital assets amounted to \$12,759,017, of which \$7,730,811 is related to infrastructure assets at June 30, 2004. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the municipal government, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

Actual costs incurred to purchase or construct capital assets were \$329,888 for the year ended June 30, 2004. Depreciation and amortization charges for the year totaled \$886,954.

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

Debt Administration

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

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

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

ECONOMIC FACTORS AND NEXT BUDGETS AND RATES

The Municipality relies primarily on property and municipal license taxes, as well as, federal and state grants to carry out the governmental activities. Historically, property and municipal license taxes have

been very predictable with increases not generally exceeding ten percent. Federal grant revenues may vary if new grants are available but the revenue is also very predictable.

Those factors were considered when preparing the Municipality's budget for the 2003-2004 fiscal year. There were no significant changes between the budget for fiscal year 2002-2003 and the one for fiscal year 2003-2004.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayers, customers, investors and creditors) with a general overview of the Municipality's finances and demonstrate the Municipality's accountability. If you have any questions about the report or need additional financial information, contact the Municipality's Director of Finance, Mr. Norberto Acevedo Vales, at Box 539, Camuy, Puerto Rico, 00627-0539.

Commonwealth of Puerto Rico
Municipality of Camuy
Statement of Net Assets
June 30, 2004

Assets	Governmental Activities
Current assets:	
Cash with commercial banks	\$ 673,225
Accounts receivable:	
Property taxes, net of allowance for doubtful accounts of \$1,747,313	2,005,784
Grant and contributions	1,922,497
Investments	506,342
Restricted assets :	
Cash with commercial banks	-
Cash with fiscal agent	456,772
Property taxes, net of allowance for doubtful accounts of \$379,397	462,834
Total current assets	<u>6,027,454</u>
Noncurrent assets:	
Capital assets, net of accumulated depreciation and amortization of \$12,759,017	18,611,781
Total noncurrent assets	<u>18,611,781</u>
Total assets	<u>\$ 24,639,235</u>

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

Commonwealth of Puerto Rico
Municipality of Camuy
Statement of Net Assets(continued)
June 30, 2004

Current liabilities (due within one year):		
Accounts payable	\$	341,074
Intergovernmental payables		4,337,498
Accrued employees' christmas bonus		152,398
Accrued interest payable on long-term debt		73,344
Deferred revenues		706,795
Current portion of long-term obligations		
Bonds payable		220,000
Notes payable		102,472
Compensated absences		805,668
Claims and judgments		209,873
Total current liabilities		<u>6,949,122</u>
Noncurrent liabilities (due in more than one year):		
Bonds payable		3,267,000
Notes payable		1,370,123
Compensated absences		528,814
Total noncurrent liabilities		<u>5,165,937</u>
Total liabilities		<u>12,115,059</u>
Net assets (liabilities):		
Invested in capital assets, net of related debt		13,595,377
Restricted for:		
Capital projects	24,794	
Debt service	156,122	
Other specified purposes	<u>3,802,824</u>	
Total restricted net assets		<u>3,983,740</u>
Unrestricted net liabilities		<u>(3,574,622)</u>
Total net assets		<u>\$ 12,524,176</u>
Total liabilities and net assets		<u><u>\$24,639,235</u></u>

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

Commonwealth of Puerto Rico
Municipality of Camuy
Statement of Activities
June 30, 2004

Functions/programs	Expenses	Charges for services	Program Revenues		Net Expenses and Charges in Net Assets
			Operating grants and contributions	Capital grants and contributions	
Governmental activities					
General government	\$ 4,651,986	36,190	284,781		\$ (4,331,015)
Urban and economic development	2,240,922				(2,240,922)
Public safety	622,129		195,864		(426,265)
Health and sanitation	1,603,564				(1,603,564)
Culture, recreation and education	647,232		75,502		(571,730)
Public housing and welfare	1,760,033		1,270,144	470,288	(19,601)
Interest on long-term obligation	181,324				(181,324)
Total governmental activities	<u>\$ 11,707,190</u>	<u>36,190</u>	<u>1,826,291</u>	<u>470,288</u>	<u>(9,374,421)</u>
General Revenues:					
Taxes:					
					6,467,096
Property taxes					502,804
Municipal license taxes					255,119
Construccion excise taxes					<u>7,225,019</u>
Total taxes					1,763,369
Grants and contributions, not restricted to specific programs					4,579
Unrestricted interests on deposits					379,484
Miscellaneous					506,343
Special items - Puerto Rico Electric Power Authority					<u>9,878,794</u>
Total general revenues and special items					504,373
Net changes in net assets					12,019,803
Net assets at beginning of the year					<u>\$ 12,524,176</u>
Net assets at the end of the year					

Commonwealth of Puerto Rico
Municipality of Camuy
 Balance Sheet - Governmental Funds
 June 30, 2004

	<u>Major Funds</u>			<u>Total Governmental Funds</u>
	<u>General Fund</u>	<u>Joint Resolution Fund</u>	<u>Other Governmental Funds</u>	
Assets				
Cash in commercial banks	\$ 98,598	1,283	573,345	\$ 673,226
Property tax receivables, net of allowances for uncollectables accounts:				
Intergovernmental	2,005,784	-	-	2,005,784
Due from other funds	409,408	3,453,182	97,983	3,960,573
Due from governmental entities	1,449,952	-	130,240	1,580,192
Due from federal financial assistance	-	-	271,521	271,521
Investments	506,342	-	-	506,342
Restricted assets:				
Cash with commercial banks	-	-	-	-
Cash with fiscal agent	3,050	-	453,722	456,772
Property taxes receivable, net of allowance for uncollectible accounts	-	-	462,835	462,835
Total assets	<u>4,473,134</u>	<u>3,454,465</u>	<u>1,989,646</u>	<u>9,917,245</u>
Liabilities				
Accounts payable	156,542	2,040	104,039	262,621
Due to other funds	3,547,186	-	413,387	3,960,573
Due to governmental entities	1,124,734	-	-	1,124,734
Deferred revenues	5,220	-	308,573	313,793
Deferred intergovernmental revenues	2,913,079	-	444,921	3,358,000
Deferred federal financial assistance	-	-	-	-
Matured bonds due and payable	-	-	293,344	293,344
Commitments and Contingencie	10,500	-	-	10,500
Total liabilities	<u>7,757,261</u>	<u>2,040</u>	<u>1,564,265</u>	<u>9,323,566</u>
Fund Balances				
Reserved for:				
Debt service	-	-	156,122	156,122
Capital projects	-	-	-	-
Other specified purposes	384,483	3,452,425	269,259	4,106,167
Unreserved, reported in:				
General fund	<u>(3,668,610)</u>	<u>-</u>	<u>-</u>	<u>(3,668,610)</u>
Total fund balances	<u>(3,284,127)</u>	<u>3,452,425</u>	<u>425,381</u>	<u>593,679</u>
Total liabilities and fund balances	<u>\$ 4,473,134</u>	<u>3,454,465</u>	<u>1,989,646</u>	<u>\$ 9,917,245</u>

Commonwealth of Puerto Rico
Municipality of Camuy
Statement of Revenues, Expenditures and
Changes in Fund Balances - Governmental Funds
Year Ended June 30, 2004

	<u>Major Funds</u>			<u>Total Governmental Funds</u>
	<u>General Fund</u>	<u>Joint Resolution Fund</u>	<u>Other Governmental Funds</u>	
Revenues:				
Taxes				
Property taxes	\$ 6,081,936			\$ 6,081,936
Municipal license taxes	502,804			502,804
Construction excise taxes	255,119			255,119
Charges for services	36,190			36,190
Intergovernmental grants and contributions				
Federal government			1,914,913	1,914,913
State government	1,134,082	2,200	936,570	2,072,852
Investment earnings	4,579	-	160	4,739
Miscellaneous	364,122	3	15,359	379,484
Total revenues	<u>8,378,832</u>	<u>2,203</u>	<u>2,867,002</u>	<u>11,248,037</u>
Expenditures:				
Current				
General government	3,910,607		284,780	4,195,387
Urban and economic development	1,587,998	-	42,189	1,630,187
Public safety	444,937		149,004	593,941
Health and sanitation	1,530,985		-	1,530,985
Culture, recreation and education	457,175		68,301	525,476
Public housing and welfare	-	53,517	1,699,807	1,753,324
Debt service:				
Principal	-		250,882	250,882
Interest	-		174,013	174,013
Capital outlays				
Construction and remodeling of public facilities	19,342	-	52,650	71,992
Total expenditures	<u>7,951,044</u>	<u>53,517</u>	<u>2,721,626</u>	<u>10,726,187</u>
Excess (deficiency) of revenues over (under) expenditures	<u>427,788</u>	<u>(51,314)</u>	<u>145,376</u>	<u>521,850</u>
Other financing sources (uses):				
Transfers-in from other funds	-		30,750	30,750
Transfers-out to other funds	(30,750)		-	(30,750)
Total other financing sources (uses), net	<u>(30,750)</u>	<u>-</u>	<u>30,750</u>	<u>-</u>

Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing uses	397,038	(51,314)	176,128	521,850
Special items - gain (loss)				
Proceeds on legal settlement award	532,992			532,992
Payment on legal case settlement award	<u>(26,650)</u>			<u>(26,650)</u>
Total special items, net	<u>506,342</u>	<u>-</u>	<u>-</u>	<u>506,342</u>
Excess (deficiency) of revenues and other financing sources and special itmes over (under) expenditures and other financing uses	903,380	(51,314)	176,128	1,028,194
Fund Balance (deficit) at beginning of year, as restated	<u>(4,187,507)</u>	<u>3,503,739</u>	<u>249,252</u>	<u>(434,516)</u>
Fund Balance (deficit) at end of year	<u>\$ (3,284,127)</u>	<u>3,452,425</u>	<u>425,381</u>	<u>\$ 593,679</u>

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

Commonwealth of Puerto Rico
Municipality of Camuy
 Reconciliation of the Balance Sheets-Governmental Funds
 to the Statements of Net Assets
 June 30, 2004

Aggregate fund balance reported in the balance sheets - governmental funds \$ 593,679

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

Capital assets used in governmental activities are not financial resources, therefore are not reported in the governmental funds 18,611,781

Deferred revenues in the governmental funds that are recognized as revenues in the statements of activities 2,964,997

The following liabilities are not due (mature) in the current period, therefore are not reported in the governmental funds:

Accounts payable and accrued liabilities and interest	(414,418)
Intergovernmental payables	(4,337,498)
Bonds and notes payables	(3,487,000)
Compensated absences	(1,334,482)
Claims and judgments	(199,374)
Other reconciling items	<u>126,491</u>
Governmental activities net assets reported in statements of net assets	<u><u>\$ 12,524,176</u></u>

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

Commonwealth of Puerto Rico
Municipality of Camuy
 Reconciliation of Statement of Revenues, Expenditures and Changes
 in Fund Balance - Governmental Funds to the Statements of Activities
 June 30, 2004

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

Excess of revenues, other financial sources and special items over expenditure and other financial uses, as reported in the accompanying statement of revenues, expenditures and change in fund balance - governmental funds	\$ 1,028,193
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The following revenues recorded in the statement of activities do not provide current financial resources, therefore are deferred in

Property taxes	385,160
Intergovernmental grants and contributions	72,022

Governmental funds report capital outlays as expenditures. However in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation and amortization expenses. This the amount by which capital outlays exceeded depreciation and amortization expenses	71,992
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Repayment of principal of long-term obligation is an expenditures in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets	250,882
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Some expenses reported in the statements of activities do not requiere the use of currents financial resources, therefore are not reported as expenditures in the governmental funds	<u>(1,303,877)</u>
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Net changes in net assets reported in statements of activities	<u><u>\$ 504,371</u></u>
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The accompanying notes to the basic financial statements are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
Notes to Basic Financial Statements
June 30, 2004

1. Summary of Significant Accounting Policies

The Municipality of Camuy of the Commonwealth of Puerto Rico (the "Municipality") is a local government with full legislative, fiscal and administrative powers to operate as a government under Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipalities Act of the Commonwealth of Puerto Rico (Law No. 81)*.

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

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

a) New Financial Reporting Model

The accompanying basic financial statements present the financial position and the results of operations of the Municipality as a whole, and its various governmental funds as of and for the year ended June 30, 2004, in conformity with accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (GASB).

In June 1999, GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB No. 34). This statement established new financial reporting requirements for state and local governments. On July 1, 2002, the Municipality adopted the provisions of GASB No. 34 as well as other statements referred to below. These statements require the reporting of new financial information and restructured much of the information that governments have reported prior to July 1, 2002. Accordingly, comparability with financial statements issued for years ended June 30, 2002 or before, has been affected significantly.

According to the new financial reporting model established by GASB No. 34, the minimum required financial statement presentation applicable to the Municipality is composed of the following elements: (1) government-wide financial statements (GWFS), (2) governmental fund financial statements (GFFS), (3) notes to basic financial statements, and (4) required supplementary information (RSI).

The RSI, which consists of a management discussion and analysis (MD&A), is information presented along with, but separate from, the Municipality's basic financial statements. The

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
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June 30, 2004

MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the year ended June 30, 2004, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

As previously mentioned, on July 1, 2002, other statements and interpretations were also adopted in conjunction and simultaneously with GASB No. 34. Those statements and interpretations are: (1) GASB Statement No. 33 – *Accounting and Financial Reporting for Nonexchange Transactions*, (2) GASB Statement No. 37 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, (3) GASB Statement No. 38 – *Certain Financial Statement Note Disclosures* and (4) GASB Interpretation No. 6 – *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

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

b) Financial Reporting Entity

The accompanying basic financial statements include all departments, agencies and municipal entities that: (1) are under the legal and administrative control of the Mayor and (2) whose funds are under the legal custody and control of the Municipality's Director of Finance and Budget, as prescribed by Law No. 81.

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

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

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
June 30, 2004

On July 1, 2003, the Municipality adopted the provisions of GASB Statement No. 39 – *Determining Whether Certain Organizations are Component Units* (GASB No. 39). This statement provides additional guidance in determining whether certain organizations for which the primary government is not financially accountable should be reported as component units based on the nature and significance of their relationship with the primary government. Generally, GASB No. 39 requires reporting a component unit if an organization raises and holds economic resources for the direct benefit of a governmental unit.

The Municipality's management has concluded that, based on the aforementioned criteria, there are no legally separate entities or organizations that should be reported as component units of the Municipality as of June 30, 2004 nor for the year then ended.

c) *Government-wide Financial Statements*

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

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

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

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

- **Invested in capital assets, net of related debt** – These consist of capital assets, net of accumulated depreciation and amortization, reduced by the outstanding balances of bonds, notes and other debt that are attributed to the acquisition, construction or improvement of

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
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June 30, 2004

those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvement of capital assets have been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs.

- **Restricted net assets** – These consist of net assets restricted by external parties (such as creditors, grantors, contributors, laws or regulations of other governments, etc.), or net assets for which constraints are imposed by constitutional provisions or enabling legislation. Enabling legislation is defined as legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

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

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

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

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

The accompanying statement of activities presents the results of the Municipality's operations by showing how the Municipality's net assets changed during the year ended June 30, 2004, using a net (expense) revenue format. This statement presents the cost of each function/program as well as the extent to which each of the Municipality's functions, programs or other services either contributes to or draws from the Municipality's general revenues (such as property taxes, municipal license taxes, construction excise taxes, etc.).

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

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
June 30, 2004

housing and welfare. The governmental operations of the Municipality's departments and operational units are classified within the following functions/programs in the accompanying basic financial statements:

General government:

- Municipal legislature
- Mayor's office
- Department of finance and budget
- Department of human resources
- Department of municipal secretary
- Department of internal audit

Urban and economic development:

- Department of public works

Public safety:

- Department of municipal police
- Department of emergency management

Health and sanitation

- Department of health
- Department of sanitation

Culture, recreation and education:

- Department of recreation and sports
- Department of tourism

Public housing and welfare:

- Department of elderly affairs
- Department of service to citizen

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

Program revenues are generated directly from a program itself or may come from parties outside the Municipality's taxpayers or citizens. In the statement of activities, program revenues reduce

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
Notes to Basic Financial Statements
June 30, 2004

the costs (expenses) of the function/program to arrive at the net cost of the function/program that must be financed from the Municipality's general revenues. The accompanying statement of activities separately reports the following categories of program revenues:

- **Charges for services** – These generally consist of exchange or exchange-like transactions involving charges to customers or applicants who purchase, use or directly benefit from the goods, services or privileges provided, or are otherwise directly affected by the services. These include fees charged for specific services, charges for licenses and permits, and fines and forfeitures, among others.
- **Program-specific capital and operating grants and contributions** – These consist of transactions that are either mandatory or voluntary nonexchange transactions with other governments, organizations, or individuals that restrict the resources for use in a particular program. Capital grants and contributions consist of capital assets or resources that are restricted for capital purposes – to purchase, construct or renovate capital assets associated with a specific program. Operating grants and contributions consist of resources that are required to be used to finance the costs of operating a specific program or can be used either for operating or capital purposes of a specific program. Restricted capital and operating grants and contributions are program revenues because they are specifically attributable to a program and reduce the net expense of that program to the Municipality. They are reported net of estimated uncollectible amounts.

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
Notes to Basic Financial Statements
June 30, 2004

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

The Municipality has no fiduciary activities, which are those in which the Municipality would be holding or managing net assets for specific individuals or other external parties in accordance with trust agreements or other custodial arrangements. In addition, the Municipality has no operations or activities that are primarily financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public is financed primarily through user charges.

d) Governmental Fund Financial Statements

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

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

- **General fund** – The general fund is the Municipality's main operating and major fund, as defined below, used to account for all financial resources and governmental activities, except for financial resources required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) GAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund.
- **Special revenue funds** – The special revenue funds are Major funds, as defined below, used by the Municipality to account for revenues derived from grants or other revenue sources

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
Notes to Basic Financial Statements
June 30, 2004

(other than major capital projects) that are either self-restricted by the Municipality or legally restricted by outside parties for use in specific purposes. The uses and limitations of each special revenue fund are specified by municipal ordinances or federal and state statutes. However, resources restricted to expenditure for purposes normally financed from the general fund are reported in the Municipality's general fund provided that all applicable legal requirements are appropriately satisfied. In this case, a special revenue fund to account for such kind of transactions will be used only if legally mandated.

- **Debt service fund** – The debt service fund is a Nonmajor fund, as defined below, used by the Municipality to account for the accumulation of resources for, and the payment of, principal and interest for: (1) bonds and notes for which debt service payments are legally mandated to be accounted for in a debt service fund and/or (2) general long-term debt for which the Municipality is being accumulating financial resources in advance, to pay principal and interest payments maturing in future years. Principal and accrued interest due on July 1 of the following fiscal year related to long-term debt for which debt service payments are accounted for in the debt service fund, are recorded as debt service fund's liabilities at June 30, if resources are available at June 30 for its payment.

General long-term debts for which debt service payments do not involve the advance accumulation of resources (such as obligations under capital leases, compensated absences, claims and judgments, and notes payable, among others) are accounted for in the accompanying statement of net assets. The debt service payments of such debts are generally accounted for in the general fund.

- **Capital projects funds** – Capital projects funds are major and nonmajor funds, as defined below, used to account for the financial resources used in the acquisition or construction of major capital facilities, other assets and permanent improvements. Significant capital outlays financed from general obligation bond proceeds are accounted for also in the capital projects funds.

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

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

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
June 30, 2004

in the governmental fund financial statements, while data from all nonmajor governmental funds are aggregated into a single column, regardless of fund type.

By definition, the Municipality's general fund is always considered a major governmental fund for financial reporting purposes. In addition, any other fund is considered a major fund for financial reporting purposes if its total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding element total (assets, liabilities, revenues or expenditures) for all governmental funds. For the purposes of applying the aforementioned major fund criteria, no eliminations of interfund balances have been made. Total revenues for these purposes means all revenues, including operating and nonoperating revenues (net of allowances), except for other financing sources. Total expenditures for these purposes means all expenditures, including operating and nonoperating expenditures, except for other financing uses.

Based on the aforementioned criteria, the Municipality's major governmental funds reported in the accompanying governmental fund financial statements are: (1) the general fund and (2) the state legislative joint resolutions fund.

The state legislative joint resolutions fund is a major fund used to account for financial resources derived from capital and operating grants awarded each year by the Commonwealth's Senate and House of Representatives (the Commonwealth's Legislature). The purpose of the amounts awarded by the Commonwealth's Legislature vary from year to year, but are generally restricted to (1) partially subsidize certain qualifying administrative and operational activities of the Municipality, (2) provide specific multipurpose services to citizens and (3) finance the acquisition or construction of capital assets approved by the Commonwealth's Legislature.

e) Measurement Focus and Basis of Accounting

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

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

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June 30, 2004

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

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

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

Government-mandated nonexchange transactions (such as grants and contributions) result when a government at one level (such as the federal or state government) provides resources to another government (such as the Municipality), and the provider government requires the recipient government to use those resources for a specific purpose or purposes established in the provider's enabling legislation. In these type of transactions, receivables and revenues are generally recorded as follows:

- For reimbursement-type (commonly known as "expenditure-driven awards"), receivables and revenues are recorded when all eligibility requirements imposed by the provider have been met. The Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Revenue is, therefore, generally recognized as qualifying reimbursable expenditures are incurred.
- For other types of grants (mainly grants and contributions with purpose restrictions but with no time requirements), receivables and revenues are recorded when all applicable eligibility requirements are met. When the provider is a government (including the government of the United States of America) the applicable recognition period for both, the provider and the recipient, is the provider's fiscal year and begins on the first day of that year.

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

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

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

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

Governmental fund financial statements – The accompanying GFFS are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available. Revenues are generally considered to be available when they are collectible within the current year or soon enough thereafter to pay liabilities of the current year. For this purpose, the Municipality considers most revenues to be available if collected within 90 days after June 30, 2004, except for property taxes for which the availability period is 60 days. Revenue sources not meeting this availability criterion or collected in advance are recorded as deferred revenues at June 30, 2004. The principal revenue sources considered susceptible to accrual include property taxes, municipal license taxes, intergovernmental grants and contributions and interest income. These principal revenue sources meet both measurability and availability criteria in the accompanying GFFS, except for amounts recorded as deferred revenues.

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

All revenues, expenses, gains, losses and assets resulting from nonexchange transactions are recorded in a similar manner to the GWFS, using the previously discussed criteria set forth by GASB No. 33 for nonexchange transactions, but subject to and limited by the availability criteria discussed above. Accordingly, municipal license tax receivables and revenues are generally recorded when the underlying exchange has occurred. Property tax receivables are also generally recorded in the period when an enforceable legal claim has arisen while property tax revenues

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(net of amounts considered not collectible) are also generally recorded in the period when resources are required to be used or the first period that the use of the resources is permitted. Receivables and revenues from reimbursement-type grants, contributions, donations and entitlements are also generally recorded as qualifying reimbursable expenditures are incurred, while receivables and revenues from other types of grants are recorded when all eligibility requirements imposed by the provider have been met.

Interest income is recorded when earned only if collected within 90 days after year-end since these would be considered both measurable and available.

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

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

Modifications to the accrual basis of accounting include:

- Employees' accumulated vacation, sick leave and compensatory time (compensated absences) is recorded as expenditure when consumed. The amount of the unpaid compensated absences has been reported only in the accompanying statements of net assets.
- Principal and interest on bonds and notes payable are recorded when they mature (when payment is due), except for principal and interest due in July 1 of the following fiscal year, which are recorded when resources are available in the debt service fund (generally June 30).
- Obligations under capital leases, amounts subject to claims and judgments under litigation and other long-term obligations are recorded only when they mature (when payment is due).
- Accounts payable and accrued liabilities not expected to be liquidated with available and expendable financial resources are recorded in the accompanying statement of net assets but not in the governmental funds.
- Executory purchase orders and contracts are recorded as a reservation of fund balance in the GFFS.

Liabilities outside the bounds of these exceptions or modifications are reported as governmental fund liabilities when incurred (including salaries, professional services, supplies, utilities, etc.)

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since these liabilities normally are paid in a timely manner and in full from current financial resources.

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

Under the new financial reporting model established by GASB No. 34, all general capital assets and the unmatured long-term liabilities (determined using the modified accrual basis of accounting) are no longer reported in account groups within the governmental fund balance sheet but are incorporated into the accompanying statement of net assets since July 1, 2002.

f) Stewardship, Compliance and Accountability

Budgetary Control

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

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

The Municipal Legislature has 10 business days, up to June 13, to discuss and approve the Project with modifications. The Municipal Legislature may amend the budgets submitted by the Mayor but may not increase any items so far to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. After the Municipal Legislature modifies and preliminarily approves the Project, the modified Project is sent back to the Mayor for his approval or rejection within 6 days. The Mayor may decrease or eliminate any line item but may not increase or insert any new line item in the budgets. The Mayor may also veto the budgets in their entirety and return it to the Municipal Legislature with his objections. If the Mayor rejects the Project, the Municipal Legislature will have up to 8 days to adopt or reject the recommendations or objections of the Mayor. The approved Project is sent again to the Mayor, which then would have 3 days to sign and approve it.

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

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

The Municipality's Department of Finance and Budget has the responsibility to ensure that budgetary spending control is maintained. For day-to-day management control, expenditures plus encumbrances may not exceed budgeted amounts at the expenditure-type level of each cost center (activity within a program within a fund). The Mayor may transfer unencumbered appropriations within programs within funds. The Municipal Legislature may transfer amounts among programs within and among funds.

The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriation) is at the functions/program level (general government, urban and economic development, public safety, health and sanitation, culture, recreation and education, and public housing and welfare) within a fund.

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

Budgetary Accounting

The Municipality's annual budgets are prepared under the budgetary (statutory) basis of accounting, which is not in accordance with GAAP.

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

The Municipality uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control. Accordingly, expenditures are generally recorded when the related expenditure is incurred or encumbered. Available appropriations and encumbrances are established to lapse one year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and

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encumbrances lapse at year-end. Other appropriations, mainly capital projects appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The accompanying budgetary comparison schedule provides information about the general fund's original budget, the amendments made to such budget, and the actual general fund's results of operations under the budgetary basis of accounting for the fiscal year ended June 30, 2004. Further details of the Municipality's budgetary control at the legal level may be obtained from the Budgetary Liquidation Report for the fiscal year ended June 30, 2004, which is prepared by the Municipality's Department of Finance and Budget. Copies of that report may be obtained by writing to the Municipality's Director of Finance and Budget.

Accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present the governmental fund financial statements in conformity with GAAP. Accordingly, the accompanying budgetary comparison schedule is accompanied by a reconciliation of the differences between the budgetary basis and GAAP actual amounts.

The Municipality does not legally adopt budgets for the state legislative joint resolutions capital fund. The financial resources received by these funds are not subject to budgeting by the Municipality since the resources received each year from the respective grantors vary from year to year, and the respective amounts are granted at their discretion.

g) Unrestricted and Restricted Deposits

The Municipality's deposits are composed of cash on hand, demand deposits and cash equivalents in: (1) commercial banks, (2) the Government Development Bank for Puerto Rico (GDB), a governmental bank and a major component unit of the Commonwealth, who is statutorily designated as fiscal agent of the Municipality, and (3) the Municipal Revenue Collection Center (CRIM, by its Spanish acronyms), a governmental entity responsible for the imposition and collection of property taxes on behalf of all municipalities of Puerto Rico.

The Municipality follows the practice of pooling cash. The balance in the pooled cash account is available to meet current operating requirements. Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the federal depository insurance generally provided by the Federal Deposits Insurance Corporation (FDIC). All securities pledged as collateral are held by agents designated by the Secretary of the Treasury of the Commonwealth, but not in the Municipality's name.

Restricted assets include cash and cash equivalents in commercial banks, GDB and CRIM. These cash balances are classified as restricted assets since its use is limited for the specified purposes discussed below, which are established by applicable agreements or required by law.

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Restricted cash with fiscal agent in the general and debt service funds represent property tax collections which are retained and restricted for the payment of the Municipality's debt service, as established by law. Restricted cash in fiscal agent in other governmental funds consists of unspent proceeds of bonds and notes, and the balance of interest and noninterest bearing accounts which are restricted for: (1) the acquisition, construction or improvement of major capital assets and the operations of federal and state funded programs.

h) Unrestricted and Restricted Accounts and Notes Receivable

In the accompanying GWFS, receivables consist of all revenues earned but not collected at June 30, 2004. Major receivable balances for the governmental activities include municipal license taxes, property taxes and intergovernmental receivables.

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

Intergovernmental receivables are composed of: (1) amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federal and state funded programs (recorded in the general fund, special revenue funds and capital project funds), and (2) contributions in lieu of taxes from the Puerto Rico Electric Power Authority, recorded in the general fund.

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

Activities among funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e. the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Advances between funds, as reported in the GFFS, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

i) Inventories and Other Current Assets

Inventories and other current assets consist of materials, supplies, food and medicine inventories held for consumption; and prepaid costs. Generally, inventories and other current assets are capitalized (consumption method). Inventories are stated at cost using the first-in, first-out method (FIFO).

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j) Deferred Charges

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

k) Capital Assets

Capital assets used in governmental activities include land and land improvements, buildings, structures and building improvements, machinery and equipment, furniture and fixtures, licensed vehicles, construction in progress, and infrastructure. These assets are capitalized and reported in the accompanying statement of net assets. Infrastructure assets are generally stationary in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets.

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

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

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

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

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	<u>Years</u>
Land improvements	20
Buildings, structures and building improvements	30 to 50
Infrastructure	20 to 50
Licensed vehicles	8
Furniture and fixtures	5 to 20
Machinery and equipment, excluding those held under capital leases	5 to 20

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

l) Deferred Revenues

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

- Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period. As previously discussed, available is defined as due (or past due) at June 30, and collected within 90 days (60 days for property taxes) thereafter to pay obligations due at June 30, or;
- The Municipality receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, the liability for deferred revenue is removed and revenue is recognized.

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

m) Compensated Absences

Compensated absences are accounted for under the provisions of Statement No. 16, *Accounting for Compensated Absences*, issued by GASB (GASB No. 16). Compensated absences include paid time off made available to employees in connection with vacation, sick leave and compensatory time. The liability for compensated absences recorded in the accompanying statement of net assets is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2004 and (2) is not contingent on a specific event (such as illness) that is outside the control of the Municipality and the employee. The liability for compensated absences

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includes salary-related costs, which are directly and incrementally related to the amount of salary paid to the employee (such as employer's share of social security taxes and medicare taxes).

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

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

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

n) Long-term Debt

The long-term liabilities reported in the accompanying statements of net assets include the Municipality's bonds, notes, obligation under capital leases, compensated absences and legal claims and judgments.

All long-term debt to be repaid from governmental resources is reported as liabilities in the accompanying statement of net assets. Principal and interest payments on bonds due in July 1 of the following fiscal year, are recorded as fund liabilities in the GFFS when resources are available in the debt service fund (generally at June 30). In the GFFS, the face amount of debt issued is reported as other financing sources when issued.

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

On July 1, 2002, the Municipality adopted the provisions of APB Opinion No. 21, *Interest on Receivables and Payables* (APB No. 21), to account for certain non-interest bearing notes payable to: (1) CRIM, (2) Puerto Rico Land Authority and Puerto Rico Aqueduct and Sewer Authority, two discretely presented component units of the Commonwealth, and (3) Puerto Rico

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Treasury Department and Puerto Rico Department of Labor and Human Resources, two agencies (governmental units) of the primary government of the Commonwealth.

According to APB No. 21, the Municipality has recorded such notes at present value with an imputed interest rate that approximates the rate that would have been used, using the same terms and conditions, if it had been negotiated by an independent lender. In the accompanying statement of net assets, such notes payable are reported net of the applicable unamortized discount, which is the difference between the present value and the face amount of the notes. The notes discount is amortized over the life of the notes using the effective interest method. Amortization of the notes discount is recorded as part of interest expense in the statement of activities. In the GFFS, notes discount is recognized as other financing uses during the current period.

o) Accounting for Pension Costs

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

According to GASB No. 27, the Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

p) Risk Management

The Municipality carries commercial insurance covering casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department (the Treasury Department) on behalf of all municipalities of Puerto Rico. The Treasury Department pays the insurance premiums on behalf of the Municipality and then is reimbursed each year through monthly equal payments deducted from the Municipality's gross property tax collections made by CRIM.

The Municipality carries insurance coverage for death and bodily injuries caused by automobile accidents. This insurance is obtained through the Automobile Accidents Compensation Administration ("ACAA", by its Spanish acronym), a discretely component unit of the

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Commonwealth. This insurance is compulsory for all licensed vehicles used on public roads and highways in Puerto Rico. The annual premium is \$35 per licensed motor vehicle, which is paid directly to ACAA.

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

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

The Municipality also obtains medical insurance coverage for its employees. The current insurance policies have not been canceled or terminated at June 30, 2004. In the past three years, the Municipality has not settled claims that exceeded insurance coverage.

q) Reservations of Fund Balances

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

- **Encumbrances** – Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts represent reservations of unexpired appropriations and generally will become liabilities in future periods as the goods or services are received.
- **Capital Projects** – Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
- **Debt Service** – Represent fund balances available to finance future debt service payments.
- **Advances** – Represent the reservation of resources set aside for long-term accounts, notes and interfund receivables, which are not considered current available financial resources.

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- *Inventories and other current assets* – Represent the reservation of resources set aside for inventories and prepaid costs, which are not considered current available financial resources.
- *Other Specified Purposes* – Represent resources set aside for use in federal and state grant programs accounted for in the special revenue funds.

r) *Interfund Activities*

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

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

In the GFFS, interfund activity has not been eliminated, as permitted by GAAP.

s) *Use of Estimates*

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

t) *Future Adoption of Accounting Pronouncements*

On March 27, 2003, the GASB issued its Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate, (3) investment maturity, (4) interest rate sensitivity and (5) foreign exchange exposure. The provisions of GASB No. 40 are effective for the Municipality's fiscal year commencing on July 1, 2004.

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On November 18, 2003, the GASB issued its Statement No. 42 (GASB No. 42), *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. This statement requires governments to report the effects of capital asset impairment in their financial statements. This statement also requires all governments to account for insurance recoveries in the same manner. The provisions of GASB No. 40 are effective for the Municipality's fiscal year commencing on July 1, 2005.

The Municipality's management has concluded that the future adoption of GASB Statements No. 40 and 42, will not have a significant impact on the Municipality's basic financial statements.

2. DEPOSITS

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

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

The Municipality's bank balance of deposits with financial institutions is categorized to provide an indication of the level of collateral risk assumed by the Municipality at June 30, 2004. Risk categories are described as follows:

- Category 1:** Deposit is insured or collateralized with securities held by the Secretary of the Treasury' agents in the Municipality's name.
- Category 2:** Deposit is collateralized with securities held by pledging financial institution's trust department or agent in the Municipality's name.
- Category 3:** Deposit is uncollateralized; including any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the Municipality's name.

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The carrying amount (book balance) of cash and cash equivalents at June 30, 2004 consist of the following:

	<u>General fund</u>	<u>State legislative joint resolutions fund</u>	<u>Nonmajor funds</u>	<u>Totals</u>
Unrestricted (category 1):				
Cash in commercial banks	\$ 29,615	-	-	\$ 29,615
Restricted (category 1):				
Cash in commercial banks	107,431	1,283	574,960	683,674
Restricted (category 3):				
Cash in GDB or CRIM, as fiscal agents	<u>3,050</u>	<u>-</u>	<u>453,722</u>	<u>456,772</u>
Total deposits	<u>\$140,096</u>	<u>1,283</u>	<u>1,028,682</u>	<u>\$1,170,061</u>

The Municipality's bank balances in commercial banks amounting to \$2,543,488 at June 30, 2004 were fully collateralized (Category 1). The bank balance of deposits in GDB and CRIM, which is uninsured and uncollateralized (Category 3), amounted to \$633,298 at June 30, 2004.

3. MUNICIPAL LICENSE TAXES

The Municipality is authorized by Law No. 81 to impose and collect municipal license taxes on all trade or business activities operated by any natural or legal person within the territorial area of Camuy. This is a self-assessed tax generally based on the business volume measured by gross sales. The Municipality establishes the applicable tax rates. At June 30, 2004, the municipal tax rates imposed by the Municipality were 1.50% for financing institutions and 0.50% for other types of taxpayers. Any taxpayers that have been granted with partial tax exemptions under any of the incentive tax laws of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60% and 90% under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return to be filed every April 15 based on the actual volume of business generated in the preceding calendar year. Taxpayers with a sales volume of \$1 million or more must include audited financial statements with their tax returns. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration. The

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first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to pay the tax in full on the filing date of the declaration (generally April 15), a 5% discount is granted automatically on the total tax amount due.

Any municipal license taxes collected in advance (that is, pertaining to a future period) are recorded as deferred revenues. Deferred municipal license tax revenues recorded in the accompanying GWFS and GFFS amounted to \$393,002 at June 30, 2004, which represents municipal licenses collected in advance for the taxable year 2004-2005.

4. PROPERTY TAXES

The Municipality is authorized by Law No. 81 to impose and collect personal and real property taxes. Under the laws and regulations of the Commonwealth, personal property taxes can be imposed to any natural or legal person that at January 1 of each year is engaged in trade or business and is the owner of personal property used in trade or business.

Personal property taxes are self-assessed by taxpayers every year generally using the book value of personal property assets owned by the taxpayer at January 1 (assessment date) and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. The total personal property tax rate in force at June 30, 2004 was 6.18% (of which taxpayers pay 5.98% and 0.20% is reimbursed by the Department of Treasury). Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property deflated to 1957 market prices. The total real property tax rate in force at June 30, 2003 was 8.18% (of which 7.98% is paid by taxpayers and 0.20% is also reimbursed by the Department of Treasury).

Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value (at 1957 market prices). For such exempt amounts, the Department of Treasury assumes payment of the basic tax (4% and 6% for personal and real property, respectively) to the Municipality, except for property assessed of less than \$3,500 (at 1957 market prices), for which no payment is made.

CRIM is responsible for the billing and collections of real and personal property taxes on behalf of the Municipality. Prior to the beginning of each fiscal year, CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, CRIM advances funds to the Municipality based on the initial estimated collections. CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than each December 31. If CRIM remits to the Municipality property tax advances, which are less than the property tax actually collected, an additional property tax receivable is recorded at June 30. However, if advances exceed the amount actually collected by CRIM, an intergovernmental payable is recorded at June 30.

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Law No. 81 provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. Such special tax is levied and collected by CRIM. Collections of this special tax are remitted to the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth.

In addition, 1.35% of the total personal and real property taxes collected by CRIM is restricted for the Municipality's debt service requirements and is retained by GDB for such purposes.

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

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

Total property tax receivable, net of an allowance for uncollectible accounts of \$2,126,710, amounted to \$2,468,618 at June 30, 2004. The composition of the property tax receivable and the related allowance for doubtful accounts is as follows:

	General fund	Debt service fund	Total
Property tax receivable	\$ 3,753,097	\$ 842,231	\$ 4,595,328
Allowance for doubtful accounts	(1,747,313)	(379,397)	(2,126,710)
Net property tax receivable	<u>\$ 2,005,784</u>	<u>462,834</u>	<u>\$ 2,468,618</u>
 Deferred (unavailable) property tax revenues in GFFS	 <u>\$ 1,937,459</u>	 <u>444,921</u>	 <u>\$ 2,382,380</u>

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5. INTERFUND BALANCES

On July 1, 2001 the Municipality adopted the provisions of Statement No. 38, *Certain Financial Statement Note Disclosures*, issued by the Governmental Accounting Standards Board. This statement requires the disclosure of the flow of resources between funds and to assess the collectibility of interfund balances. Interfund balances at June 30, 2004 consisted of the following:

	Operating transfers-in:			
	Major funds			
	General fund	State legislative joint resolutions fund	Other	Total
Operating transfers-out:				
Major funds:				
General fund	\$ -	-	30,750	\$ 30,750
State legislative joint resolutions fund	-	-	-	-
Nonmajor governmental funds	-	-	-	-
Total	\$ -	-	30,750	\$ 30,750

	Due/advances from:			
	Major funds			
	General fund	State legislative joint resolutions fund	Nonmajor governmental funds	Total
Due/advances to:				
Major funds:				
General fund	\$ -	3,453,182	94,004	\$ 3,547,186
State legislative joint resolutions fund	-	-	-	-
Nonmajor governmental funds	409,408	-	3,979	413,387
Total	\$ 409,408	3,453,182	97,983	\$ 3,960,573

At June 30, 2004 all amounts due to among funds are considered collectible by the Municipality's management.

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6. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2004, was as follows:

<u>COST BASIS</u>	Balance at June 30, 2003, as restated	Additions/ increases	Disposals/ decreases	Balance at June 30, 2004
Cost basis of capital assets, not subject to depreciation and amortization:				
Land	\$ 3,347,061	-	-	\$ 3,347,061
Construction in progress	1,698,030	71,991	-	1,770,021
Total cost basis of capital assets, not subject to depreciation and amortization	5,045,091	71,991	-	5,117,082
Cost basis of capital assets, subject to depreciation and amortization:				
Buildings, structures and building improvements	7,893,543	-	-	7,893,543
Infrastructure	13,175,524	110,891.00	-	13,286,415
Land Improvements	2,123,276	-	-	2,123,276
Licensed vehicles	1,744,656	95,070	-	1,839,726
Machinery and equipment	1,058,821	51,935	-	1,110,756
Equipment under capital leases	-	-	-	-
Total cost basis of capital assets subject to depreciation and amortization	25,995,820	257,896	-	26,253,716
Total cost basis of capital assets	\$ 31,040,911	329,887	-	\$ 31,370,798
	Balance at June 30, 2003	Depreciation and Amortization Expense	Reclassifications	Balance at June 30, 2004
<u>ACCUMULATED DEPRECIATION AND AMORTIZATION</u>				
Buildings, structures and building improvements	\$ 1,789,553	138,378	-	\$ 1,927,931
Infrastructure	7,223,070	507,741	-	7,730,811
Land Improvements	1,089,537	80,637	-	1,170,174
Licensed vehicles	1,044,631	115,918	-	1,160,549
Machinery and equipment	725,272	44,280	-	769,552
Equipment under capital leases	-	-	-	-
Total accumulated depreciation and amortization	11,872,063	886,954	-	12,759,017
CAPITAL ASSETS, NET	\$ 19,168,848	-557,067	-	\$ 18,611,781

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

General government	\$ 46,987
Public safety	28,188
Public housing and welfare	6,710
Culture and education	121,756
Health and sanitation	72,579
Urban and economic development	<u>610,735</u>
 Total depreciation and amortization expense	 <u>\$ 886,955</u>

7. EMPLOYEES RETIREMENT SYSTEM

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

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

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

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

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

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System 2000 is a hybrid defined contribution plan, also known as cash balance plan. Under this new plan, there is a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. The Commonwealth nor the Municipality will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employees' contribution (with a minimum of 8.275 percent of the employees' salary up to a maximum of 10.00 percent) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity U.S. Treasury Note; (2) earn a rate equal to 75 percent of the return of the System 2000's investment portfolio (net of management fees); or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employer's contributions (9.275 percent of the employees' salary which is applicable to the Municipality) will be used to fund the current plan.

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

Funding Policy:

Contribution requirements are established by law and are as follows:

Municipality	9.275% of gross salary
Employees:	
Hired on or before March 31, 1990	5.775% of gross salary up to \$6,600
	8.275% of gross salary over \$6,600
Hired on or after April 1, 1990	8.275% of gross salary

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

Historically, the Commonwealth has reported the System as a single-employer plan (as relates only to the financial reporting entity of the Commonwealth) in its comprehensive annual financial report. Accordingly, any actuarial deficiency that may exist or arise related to the Municipality's participating employees will be assumed by the Commonwealth since the System does not allocate any actuarial deficiencies pertaining to municipal employees participating in the System. The Municipality is only required by law to make statutory contributions in the rates mentioned above. As a result, no net pension obligation nor net pension asset that may be allocable to the

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Municipality's participating employees, if any, has been recorded in the accompanying basic financial statements.

The Municipality's actual contributions for the current and the previous two fiscal years, which are equal to the statutory required contributions, were as follows:

<u>Fiscal year ended June 30,</u>	<u>Act No. 447</u>	<u>System 2000</u>
2004	\$169,592	\$74,481
2003	\$174,590	\$4,384

8. LONG-TERM DEBT

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

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

In addition, before any new bonds or notes are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. At June 30, 2004, the Municipality is in compliance with the debt limitation requirements. The general long-term debt activity for the year ended June 30, 2004 was as follows:

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	Balance at June 30, 2003, as restated	Borrowing s or Additions	Payments or Deduction s	Balance at June 30, 2004	Due Within One Year
Bonds payables	\$ 3,723,000	-	(236,000)	\$ 3,487,000	\$ 220,000
Notes payable to:					
Puerto Rico Department of Labor and Human Resources	45,717	-	(25,003)	20,714	20,714
Puerto Rico Aqueduct and Sewer Authority	151,188	-	(64,688)	86,500	68,678
CRIM:					
Act No. 42 - Financing agreement for the excess of property tax advances over collections through fiscal year 2000	1,028,951	-	(12,250)	1,016,701	13,079
Other - LIMS					
Financing of delinquent property tax accounts sold	348,680	-	-	348,680	-
Compensated absences	1,376,293	-	(41,811)	1,334,482	805,668
Claims and judgments	10,500	199,373	-	209,873	-
Total	\$ 6,684,329	199,373	(379,752)	\$ 6,503,950	\$ 1,128,139

a) Bonds Payable

The Municipality issues general and special (public improvements) obligations bonds and notes to provide for the acquisition and construction of major capital facilities and equipment, as well as, to cover certain operating needs. Bonds and notes payable at June 30, 2004 is composed of the following debts:

General Obligations:

1996 serial notes, original amount of \$125,000, due in annual principal installments ranging from \$5,000 to \$10,000; plus interests due in semiannual installments at variable rates not to exceed 6.58% (5.80% at June 30, 2004) through July, 1, 2015.

**Outstanding
Amount**

\$ 90,000

1997 serial bonds, original amount of \$305,000, due in annual principal installments ranging from \$25,000 to \$45,000; plus interest due in semiannual installments at variable rates not to exceed 6.50% (5.00% at June 30, 2004) through July 1, 2006.

125,000

2001 serial bonds, original amount of \$1,675,000, due in annual principal installments ranging from \$25,000 to \$145,000; plus interest due in semiannual installments at variable rates no to exceed 6.50% (5.00% at June 30, 2004) through July 1, 2026

1,625,000

2001 serial notes, original amount of \$445,000, due in annual principal installments ranging from \$45,000 to \$80,000; plus interest due in semiannual installments at variable rates no to exceed 3.88% (2.80% at June 30, 2004) through July 1, 2008

350,000

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<u>General Obligations:</u>	<u>Outstanding Amount</u>
<u>Special Obligations Bonds:</u>	
1999 serial bonds, original issue amount of \$505,000, due in annual principal installments ranging from \$35,000 to \$65,000, plus interest due in semiannual installments at variable rates not to exceed 6.50% (5.00% at June 30, 2004) through July 1, 2008	295,000
<u>Public Improvement Bonds:</u>	
1983 serial bonds, original amount of \$180,000, due in annual principal installments ranging from \$5,000 to 11,000; plus interest due in annual installments at rates of 5.00% through January, 1, 2005	11,000
1995 serial bonds, original amount of \$350,000, due in annual principal installments ranging from \$10,000 to \$40,000; plus interest due in annual installments at rates not to exceed 6.20% (5.80% at June 30, 2004) through January 1, 2009	190,000
1998 serial bonds, original amount of \$280,000, due in annual principal installments ranging from \$7,000 to \$21,000; plus interest due in annual installments at rates of 5.25% through January 1, 2019	228,000
1998 serial bonds, original amount of \$310,000, due in annual principal installments ranging from \$7,000 to \$23,000; plus interest due in annual installments at rates of 5.12% through January 1, 2020	258,000
<u>Special Fund-Emergency Obligations:</u>	
1997 serial bonds, original amount of \$400,000, due in annual principal installments ranging from \$10,000 to \$40,000; plus interest due in semiannual installments at variable rates not to exceed 8.00% (5.00% at June 30, 2004) through July 1, 2016	315,000
Total bonds & notes payable	<u>\$ 3,487,000</u>

These bonds are payable from the ad valorem property tax of 1.67% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

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

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

Interest rates on serial bonds subject to variable rates are reviewed periodically by GDB and are based on the fluctuation of GDB's weighted average rate for its commercial paper program, not to exceed 8%. Under this program, GDB issues commercial paper in the U.S. taxable and tax-exempt markets, in the Eurodollar market and to corporations that have tax exemption under the Commonwealth's Industrial Incentives Act and qualify for benefits provided by the U.S. Internal Revenue Code Section 936.

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

<u>Year ended June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2005	\$ 253,000	166,359	\$ 419,359
2006	262,000	184,735	446,735
2007	284,000	175,169	459,169
2008	254,000	162,506	416,506
2009	266,000	152,224	418,224
2010-2014	590,000	629,528	1,219,528
2015-2019	655,000	402,504	1,057,504
2020-2024	518,000	220,423	738,423
2025-2028	405,000	40,788	445,788
Totals	<u>\$ 3,487,000</u>	<u>2,134,236</u>	<u>\$ 5,621,236</u>

b) Notes Payable to Puerto Rico Department of Labor and Human Resources

On February 12, 2002, the Municipality entered into a financing agreement with the Puerto Rico Department of Labor and Human Resources for the payment of past due unemployment insurance premiums amounting to \$64,338. The note bears interest at 7.95% and is payable in monthly installments of \$10,247, including interests, through November 18, 2004. At June 30, 2004, the outstanding principal and accrued interest balance on this note amounted to \$20714 and \$1001, respectively.

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Notes to Basic Financial Statements
June 30, 2004

Year ending June 30,	Principal	Interest	Total
2005	\$ 20,714	\$ 1,001	\$ 21,715
Total	\$ 20,714	\$ 1,001	\$ 21,715

c) Notes Payable to Puerto Rico Aqueduct and Sewer Authority

On June 30, 2002, the Municipality entered into a financing agreement with the Puerto Rico Aqueduct and Sewer Authority for the payment of past due water utilities services amounting to \$250,583. The note is payable in monthly installments of \$6,000 through July 5, 2005. The note bears no interest and has an imputed interest rate of 6.00%. It was originally recorded at its present value of \$230,970, net of an unamortized discount of \$19,613, at inception. At June 30, 2004, the balance of this note, net of the unamortized discount of \$2,663, amounted to \$69,366.

d) Notes Payable to CRIM

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

In addition, on December 16, 2002 the Municipality entered into a repayment agreement with GDB and CRIM to pay off the remaining \$1,040,424 of excess of property tax advances from fiscal year 2000 and 2001. CRIM retains the principal and interest from the property tax advances of the Municipality. The amounts retained by CRIM are remitted to CDB on July 1 of each year through July 1, 2032. The repayment agreement bears interest at variable rates determined by GDB (7.00% at June 30, 2004) but not exceeding 8.00%. The outstanding principal and accrued interest balances of the note payable to CRIM amounted \$1,016,701 and \$1,209,298 respectively, at June 30, 2004. The principal and interest maturities are as follows:

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Year ending June 30,	Principal	Interest	Total
2005	\$ 13,079	\$ 66,421	\$ 79,500
2006	13,965	65,535	79,500
2007	14,911	64,589	79,500
2008	15,921	63,579	79,500
2009	16,999	62,501	79,500
2010-2014	103,906	293,592	397,498
2015-2019	178,756	253,304	432,060
2020-2024	214,054	197,396	411,450
2025-2032	445,108	111,389	556,497
Total	<u>\$ 1,016,701</u>	<u>\$ 1,178,306</u>	<u>\$ 2,195,006</u>

Financing of delinquent property tax accounts sold – On April 22, 2002, the Municipality entered into a financing agreement with CRIM in the amount of \$251,724 for the payment of delinquent property tax account sold to private investors. The financing agreement in the form of a line of credit bearing interests at 6.50% during the first 5 years, and variable interests 125 points over LIBOR rate during the next 25 years. At June 30, 2004, the outstanding principal and accrued interest balances amounted to \$348,680 and \$425,605, respectively. The principal and interest maturities are as follows.

Year ending June 30,	Principal	Interest	Total
2005	\$ -	\$ 22,664	\$ 22,664
2006	-	22,664	22,664
2007	-	22,664	22,664
2008	-	22,664	22,664
2009	5,757	22,495	28,252
2010-2014	35,112	106,148	141,260
2015-2019	48,554	92,706	141,260
2020-2032	259,258	136,267	395,525
Total	<u>\$ 348,681</u>	<u>\$ 448,272</u>	<u>\$ 796,953</u>

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Notes to Basic Financial Statements
June 30, 2004

e) Compensated Absences

At June 30, 2004, the liability for compensated absences is composed as follows:

	<u>Due within one year</u>	<u>Due after one year</u>	<u>Total</u>
Vacations	\$ 386,878	96,585	\$483,463
Sick leave	337,150	432,229	769,379
Compensatory time	81,640		81,640
Total	<u>\$805,668</u>	<u>528,814</u>	<u>\$1,334,482</u>

9. COMMITMENTS AND CONTINGENCIES

The Municipality is defendant in various legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended, persons are authorized to sue the Municipality only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Municipality may provide its officers and employees with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the payment of such judgment.

With respects to pending or threatened litigation, the Municipality has reported liabilities of \$209,873 for awarded or anticipated unfavorable judgments as of June 30, 2004. On October 20, 2004 the court submitted an unfavorable judgement to the Municipality for payment of the amount previously stated.

The Municipality has reported, outstanding encumbrances amounting to \$384,483 in the general fund at June 30, 2004. The Municipality intends to honor these encumbrances, which will continue to be liquidated under the current year's budget during a lapse period that extends into the subsequent fiscal year.

10. RESTATEMENTS

The following schedule reconciles the June 30, 2003 fund balances as previously reported by the Municipality to the beginning fund balances, as restated:

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June 30, 2004

	June 30, 2003, fund balance, as previously reported	Reclassifications and adjustments	June 30, 2003, fund balance, as restated
Major funds:			
General fund	\$(5,911,961)	1,724,454	\$(4,187,507)
State legislative joint resolutions fund	3,503,739	-	3,503,739
Nonmajor funds:			
Other governmental fund	409,458	(160,206)	227,508
Totals	<u>\$1,998,764</u>	<u>1,564,248</u>	<u>\$(456,259)</u>

The following schedule reconciles the June 30, 2003 net assets previously reported by the Municipality to the beginning net assets, as restated in the accompanying statement of activities:

June 30, 2003, net assets, as previously reported	Reclassifications and adjustments	June 30, 2003, net assets, as restated
<u>\$10,455,554</u>	<u>1,564,248</u>	<u>\$12,019,802</u>

COMMONWEALTH OF PUERTO RICO
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Budgetary Comparison Schedule – General Fund
Year Ended June 30, 2004

	Budgeted Amounts		Actual amounts (budgetary basis) (see note 1)	Variance with final budget - over (under)
	Original	Final		
Revenues:				
Property taxes	\$ 5,311,275	5,311,275	5,674,496	\$ 363,221
Municipal license taxes	501,500	501,500	479,946	(21,554)
Construction excise taxes	500,000	500,000	265,119	
Charges for services	13,770	14,570	33,378	18,808
Intergovernmental grants and contributions	1,159,480	1,159,480	1,183,580	24,100
Federal financial assistance	-	-	-	-
Rent of property	-	-	-	-
Investment earnings	5,000	5,000	4,579	(421)
Miscellaneous	542,892	542,092	569,935	27,843
Total revenues	<u>8,033,916</u>	<u>8,033,916</u>	<u>8,211,032</u>	<u>411,997</u>
Expenditures:				
Current:				
General government	3,694,160	3,779,907	3,520,477	259,430
Urban and economic development	568,904	652,052	648,243	3,809
Public safety	547,413	424,506	424,506	-
Health and sanitation	1,669,917	1,775,717	1,775,717	-
Culture, recreation, and education	450,028	466,038	465,678	360
Public housing and welfare	1,103,494	935,696	933,274	2,423
Capital outlays	-	-	-	-
Total expenditures	<u>8,033,916</u>	<u>8,033,916</u>	<u>7,767,894</u>	<u>266,022</u>
Excess (deficiency) of revenues over expenditures	<u>\$ -</u>	<u>-</u>	<u>443,138</u>	<u>\$ 678,019</u>

Explanation of Differences:

Sources/inflows of financial resources:

Actual amounts (budgetary basis) "available for appropriations" from the budgetary comparison schedule	\$ 8,211,032
Differences - budget basis to GAAP:	
Net increase in receivables	68,324
Resources considered revenues for budgetary purposes but are not revenues for financial reporting purposes	(70,530)
Resources considered revenues for financial reporting purposes but are not revenues for budgetary reporting purposes	679,100
Total revenues as reported on the statement of revenues, expenditures and changes in fund balances - governmental funds	<u>\$ 8,887,926</u>

Uses/outflows of financial resources:

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	\$ 7,767,894
Differences - budget basis to GAAP:	
Net increase in payables	224,683
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	
Outflows of budgetary resources used for financing expenditures that are not expenditures for budgetary purposes	(465,294)
Outflows considered expenditures for financial reporting purposes but are not outflows for budgetary reporting purposes	437,737
Total expenditures as reported on the statement of revenues, expenditures and changes in fund balances - governmental funds	<u>\$ 7,965,020</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2004**

<u>FEDERAL GRANTOR/ PROGRAM TITLE</u>	<u>FEDERAL CFDA NUMBER</u>	<u>EXPENDITURES</u>
US DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT (HUD)		
Direct Programs:		
Housing Choise Voucher	14.871 MP	\$ 688,932
Indirect Program:		
Passed through P.R. Office of Municipal Affairs State Block Grant Program (SBGP)	14.228 MP	604,602
Total US Department of Housing and Urban Development		<u>1,293,534</u>
US DEPARTMENT OF HEALTH AND HUMAN SERVICES (HHS)		
Passed through Administration of Families and Children		
Child Care and Development Block Grant	93.575	335,844
Total US Department of Health and Human Services		<u>335,844</u>
US DEPARTMENT OF TRANSPORTATION		
Passed through PR Highway Authority		
Federal Transit Capital Improvements Grants	20.500	9,730
Total US Department of Transportation		<u>9,730</u>
US DEPARTMENT OF JUSTICE		
Direct Program:		
Public Safety Partnership and Community Policing Grants (Cops)	16.710	144,819
Total US Department of Justice		<u>144,819</u>
US DEPARTMENT OF AGRICULTURE		
Passed through PR Department of Education		
Child and Adult Care Food Program	10.558	37,578
Total US Department of Agriculture		<u>37,578</u>
TOTAL FEDERAL FINANCIAL ASSISTANCE		<u>\$ 1,821,505</u>

MP = Major Program

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004**

NOTE 1. GENERAL

The accompanying Schedule of Expenditures of Federal Awards presents balance expended of all Federal Financial Assistance Programs of the Municipality of Corozal, Puerto Rico. The reporting entity is defined in Note 1 to the general-purpose financial statements.

NOTE 2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Federal financial assistance revenues and expenditures are reported in the Municipality's general-purpose financial statements as other governmental funds and capital project fund.

NOTE 3. FEDERAL CFDA NUMBER

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

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

To the Honorable Mayor and
the Municipal Assembly
Municipality of Camuy
Camuy, Puerto Rico

We have audited the financial statements of the Municipality of Camuy as of and for the year ended June 30, 2004, and have issued our report thereon dated December 16, 2004. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Municipality of Camuy financial statements are free of material misstatement, We performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statements amounts. However, providing and 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 my tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items section in III.

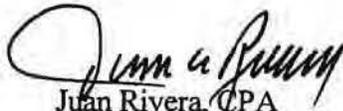
Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Municipality of Camuy 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 assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that our 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 of Camuy ability to record, process, summarize, 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 questioned costs in section III.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the 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 the 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 weakness. However, we believe that none of the reportable conditions described above is a material weakness.

This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities.


Juan Rivera, CPA
License 2214



December 16, 2004
Toa Baja, Puerto Rico

Stamp No. 2010604 of the Puerto Rico Society of Certified Public Accountants was affixed to the record copy of this report.

JUAN A. RIVERA, CPA
CERTIFIED PUBLIC ACCOUNTANT

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

To the Honorable Mayor and
the Municipal Assembly
Municipality of Camuy
Camuy, Puerto Rico

Compliance

We have audited the compliance of Municipality of Camuy 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, 2004. The Municipality of Camuy major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Municipality of Camuy management our responsibility is to express an opinion on the Municipality of Camuy compliance based on our audit.

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

As described in section III in the accompanying schedule of findings and questioned costs, the Municipality of Camuy did not comply with requirements regarding to its Section 8 and SBGP Program Management. Compliance with such requirements is necessary, in our opinion, for the Municipality of Camuy to comply with the requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality of Camuy complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for die year ended June 30, 2004.

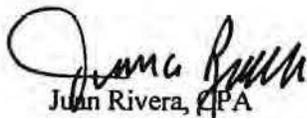
Internal Control Over Compliance

The management of the Municipality of Camuy is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, We considered the Municipality of Camuy 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.

We noted certain matters involving the internal control over compliance 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 compliance that, in our judgment, could adversely affect the Municipality of Camuy ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs section III.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

However, we believe that none of the reportable conditions described above is a material weakness. This report is intended for the information of the audit committee, the Municipality's management, the Department of Housing and Urban Development (Cognizant Agency), and federal awarding agencies and pass-through entities.


Juan Rivera, CPA
License 2214



December 16, 2004
Toa Baja, Puerto Rico

Stamp No.. 2010605 of the Puerto Rico Society of Certified Public Accountants was affixed to the record copy of this report.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED JUNE 30, 2004**

II. Schedule of Financial Statements Findings and Questioned Costs

During the examination of internal control requirements of the Municipality of Camuy, for the year ended June 30, 2004 disclosed that grants funds were generally administered in a satisfactory manner.

A. Disbursement Test

Condition 04-1

One disbursement voucher of the sample of twenty-five did not include the invoice for the services rendered.

Criteria

Based on Municipal Law Number 81 and for a good internal control, all disbursement must be justified with an certified invoice for the services rendered or goods received.

Cause

The Municipality has not established procedures to controls and records the necessary documents for disbursements.

Effect

The disbursement process may permit payments without the necessaries documents to comply with the municipality disbursement regulation.

Recommendation

The Municipality must to establish procedures in order to obtain all the documents corresponding to the disbursements before make them.

Auditee Response

The Finance Director gave instructions to the employee in charge to verified the documents for payment to enforce the current internal control system in this area to avoid this situation in the future.

Condition 04-2

One disbursement voucher of the sample of twenty-five include some invoices with corrections without explanation. In addition there are not contract between the Municipality and the services provider.

Criteria

Based on Municipal Law Number 81 and for a good internal control, the invoices should not include alterations without explanations. In addition, contract or purchase order are necessary to establish the price and condition of the purchase of services or goods.

Cause

The Municipality does not follow the actual purchase procedure.

Effect

The Municipality may pay for services or goods without properly documentation or paid improperly.

Recommendation

The Municipality must enforce the procedures to verify the disbursement documents correctly in order to avoid this situation in the future.

Auditee Response

The supplier had a standard invoice for all services and when the services were not the same, those were corrected. The Finance Director gave instructions to required original invoice for all disbursements.

Condition 04-3

Three disbursement vouchers of the sample of twenty-five include invoices dated prior the purchase orders.

Criteria

Based on the Municipal Law Number 81 and for a good internal control the purchase order must be realized first in order to certified funds available into account before the purchase.

Condition 04-3 (Cont.)

Cause

The Municipality orders the services prior to the verifications of available funds.

Effect

The Municipality commit fund without verification of availability.

Recommendation

The Municipality must enforce the purchase procedure of internal control in order to avoid this situation in the future.

Auditee Response

The Finance Director gave instructions to the people in charge of purchase to discontinued this practice immediately.

Condition 04-4

One disbursement voucher of my sample of twenty-five does not include the acceptance certification of the project that must be realized in order to pay the ten percent retained.

Criteria

Based on Municipal Law Number 81 to pay the ten percent retained to the contractor the Municipality must certify the acceptance of the project.

Cause

The Municipality did not realize the corresponding certification prior the disbursement.

Effect

The Municipality may pay of contract amount in full without proper verification that the contract was completed in satisfactory manner.

Recommendation

The Municipality must to enforce procedures in order to coordinate the acceptance of the projects.

Condition 04-4 (Cont.)

Auditee Respond:

The Finance Director gave instructions to the Pre-interventor to enforce the recommendation of the auditors immediately.

Condition 04-5

One disbursement voucher of the sample of twenty-five does not include the three quotations required from different suppliers.

Criteria

Based on Municipal Law Number 81 the Municipality must to request quotations for at least three different suppliers.

Cause

The Municipality does not request the three quotations required.

Effect

The Municipality may pay in excess for the services or goods.

Recommendation

The Municipality must enforce the actual procedures of internal control in order to avoid this situation in the future.

Auditee Response:

The Finance director gave instructions to purchase offices that three quotations are necessary for the acquisition of all services or goods.

B. Municipal Volume of Business Test

Condition 04-6

Two Municipal Volume of Business Tax Return of the sample of seventeen do not include evidence of the revenues reported on the Municipal Volume of Business Tax Declaration, such as Financial Statements or Income Tax Return.

Condition 04-6 (Cont.)

Criteria

Based on Municipal Law Number 81 the Municipal Volume of Business Tax Declaration must be included as evidence of the revenue reported such as certified Financial Statements for sales in excess of \$1 million or the revenues page of the Income Tax Return for less of \$1 million.

Cause

The Municipality did not verify correctly the document attached to the Volume of Business Tax Declarations.

Effect

The Municipality cannot verify the information submitted by tax payer are correctly and the taxes paid may be incorrectly.

Recommendation

The Municipality must establish internal control procedures in order to verify all documentation submitted by taxpayer are complete and corrected.

Auditee Response:

The Finance Director gave instructions to the Collections Area to request the document mentioned above for the proper verification of taxes computation for the year.

C. Contract Test

Condition 04-7

Exception of clauses required by the Comptroller Office in Puerto Rico:

<u>Contract Number</u>	<u>Conditions</u>
2004-89	A, B
2004-105	D
2004-139	B
2004-183	A, C
2004-239	C
2004-257	A, C
2004-297	B

- A Does not establish there are not interest conflicts.
- B Does not establish there are no pecuniary interests.
- C Does not establish the cancellation clause.
- D Does not establish the evidence of Income Tax Return Submission for the last five years.

Criteria

Based on Regulation Number 33 of the Comptroller of Puerto Rico the contracts must include some clauses to defend the better interest of the Municipality.

Cause

The Municipality did not verify the clauses of the contracts before signed and submitted to the Comptroller Office.

Effect

The Municipality does not complied with a good internal control system therefore did not protect the municipality interest.

Recommendation

The Municipality must to establish procedures to verify all necessary clauses to be included in the contracts in order to protect the Municipality interests.

Auditee Response:

The Mayor of the Municipality gave instructions to The Municipal Secretary Area in order to all contracts must be revise by the law office before final municipality officials approval

D. Bidding Test

Condition 04-8

One bid file of my sample of three does not include the evidence of bid bond submitted by the bidders.

Criteria

Based on Municipal Law Number 81 the bidders must to include a bid bond of the project with their offers.

Cause

The Municipality did not verify correctly all documents included with the offers of the bidders.

Effect

The Municipality did not complied with the bid procedures require by law to protect the municipality interest.

Recommendation

The Municipality must to verify the offers correctly in order to review all documentation necessary before make some decision about the bid.

Auditee Response

The Municipal Secretary gave instructions to verify all documents related to bidding before make some decision or accept the offer.

III. Federal Awards Findings and Questioned Costs

During the examination of compliance with federal requirements of the Municipality of Camuy, for the year ended June 30, 2004 disclosed that grants funds were generally administered in a satisfactory manner, except for the following situations:

Section 8 CFDA No. 14.855

Condition 04-1

We observed that 76 % of our sample of participants was selected from the waiting list. The Municipality should improve this procedures in order to comply with at least of 98%.

Criteria

Code of Federal Regulations requires (24 CFR 982.54 (d)(1) and 982.204(a)) the applicants and admissions should be selected from the waiting list.

Cause

Some participants were not selected from the waiting list.

Effect

The Municipality is not in compliance with federal regulations and does not give the same opportunity to all participants.

Recommendation

The Municipality should continue with the procedures of selecting from waiting list in order to give the same opportunity to all participants and to comply with federal regulations.

Condition 04-2

The Municipality should implement the reasonable written method established in the administrative plan to determine and document for each unit leased that the rent to owner is reasonable based on current rents for comparable unassisted units.

Criteria

Code of Federal Regulations (24 CFR 982.4, 982.54(d)(15), 982.158(f)(7) and 982.507) requires the Municipality determine and documented for each unit leased that the rent to owner is reasonable based on current rents for comparable unassisted units; at the time of

Condition 04-2 (Cont.)

initial leasing; if there any increase in the rent to owner; and at the HAP contract anniversary if there is a 5 % decrease in the published fair market rent (FMR) in effect 60 days before the HAP anniversary. This method must take in consideration the location, size, type, quality and the age of units, and the amenities, housing services, and maintenance and utilities provided by the owners in determining comparability and the reasonable rent.

Cause

The Municipality does not implement the reasonable rent procedures complete.

Effect

The Municipality is not in compliance with federal regulations, and cannot obtain an assurance the rent paid is reasonable.

Recommendation

The Municipality should implement as soon as possible the complete reasonable method written in the administrative plan in order to comply with federal regulations.

Condition 04-3

During the audit we observe the procedures of housing quality standards (HQS) are implemented and the deficiencies are corrected into time required, but the procedures should be improved because some deficiencies are not corrected yet in some cases.

Criteria

Code of Federal Regulation requires (24 CFR 982.404) that any cited life-threatening HQS deficiencies are corrected within 24 hours from the inspection and all the other cited deficiencies are corrected within no more than 30 calendar days from the inspection or any PHA-approved extension.

Cause

The Municipality does not give the follow-up necessary to comply with federal regulations.

Effect

The Municipality does not have the assurance that the units are secure and comply with the standards of safe place.

Condition 04-3 (Cont.)

Recommendation

The Municipality should improve more the HQS procedures in order to comply with federal regulations.

SBGP

CFDA No. 14.228

Condition 04-4

During the audit we observed there are some construction projects that require complying with Davis-Bacon Act. The federal program office did not realize the procedures of interviews and payroll reviews.

Criteria

Code of Federal Regulations (29 CFR part 5) requires contractors to work on construction contracts in excess of \$2,000 financed by federal funds must be paid wages not less than those established for the locality of the project. The Contractor should submit weekly, a copy of the payroll and the statement of compliance (certified payrolls). Some payroll interviews help to evaluate the contractors comply with regulation.

Cause

The Municipality does not have a person assigned to realize this function.

Effect

The Municipality is not in compliance with the Davis-Bacon Act.

Recommendation

The Municipality should assign these duties to a federal program employee in order to comply with federal regulations.

Condition 04-5

The federal program office does not maintain a physical inventory of the equipment acquired by federal funds.

Condition 04-5 (Cont.)

Criteria

Based on the A-102 Common rule and OMB circular A-110, equipment records shall be maintained; a physical inventory of equipment shall be taken at least once every two years and reconcile to the equipment records when federal program acquired equipment in excess of \$5,000.

Cause

The Municipality does not maintain a physical inventory.

Effect

The Municipality is not in compliance with federal regulations.

Recommendation

The Municipality should implement a physical inventory and maintained into the federal program offices in order to comply with federal regulations.

Condition 04-6

The SBGP program should to minimize the time elapsing between transfer the federal funds from agency (OCAM) and disbursement to suppliers.

Criteria

As required by Code of federal regulation (30 CFR part 205) OCAM, the Pass-through entity, established procedures to comply with requirements for cash management. OCAM establish the federal funds should be used into three to five labor days in order to maintain less than \$5,000 on the bank account.

Cause

The Municipality does not make the disbursement into the three to five labor days required.

Effect

The Municipality is not in compliance with federal regulations.

Condition 04-6 (Cont.)

Recommendation

The Municipality should establish procedures in conjunction with finance department in order to make the disbursement into the time required.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004**

<u>Program</u>	<u>Finding/Noncompliance</u>	<u>Status</u>
Section 8 CFDA No. 14.855	Condition 03-1 The actual administrative plan must be revised and updated.	Condition partially corrected
Section 8 CFDA No. 14.855	Condition 03-2 The Municipality should modify their procedures of reasonable rent.	Condition partially corrected
Section 8 CFDA No. 14.855	Condition 03-3 Files without unit inspection report required by HUD.	Condition was corrected
Section 8 CFDA No. 14.855	Condition 03-4 HQS procedures must be implemented.	Condition partially corrected
Section 8 CFDA No. 14.855	Condition 03-5 The re-examination process is not realized each year exactly.	Condition was corrected
Section 8 CFDA No. 14.855	Condition 03-6 Some documentation and information of eligibility process were not included on participant's files.	Condition was corrected
Section 8 CFDA No. 14.855	Condition 02-1 The actual administrative plan must be revised and updated.	Condition partially corrected
Section 8 CFDA No. 14.855	Condition 02-3 The Municipality has not written procedures for reasonable rent.	Condition partially corrected
Section 8 CFDA No. 14.855	Condition 02-5 Participant files without unit inspection report required by HUD.	Condition was corrected
Section 8 CFDA No. 14.855	Condition 02-6 They're no procedures of HQS deficiencies.	Condition partially corrected

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAMUY
SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2004**

<u>Program</u>	<u>Finding/Noncompliance</u>	<u>Status</u>
Section 8 CFDA No. 14.855	Condition 02-7 The participant files do not show an effective system of re-examination.	Condition was corrected
Section 8 CFDA No. 14.855	Condition 02-10 The Municipality does not maintain the required documents to support participant eligibility process.	Condition was corrected



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Gobierno Municipal de Camuy
Hon. Edwin García Feliciano, Alcalde
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Camuy, Puerto Rico 00627
Tel. 787-262-7704 • 5208 • Fax: 787-262-8554

CORRECTIVE ACTION PLAN

December 16, 2004

Cognizant or Oversight Agency for Audit:

Municipality of Camuy respectfully submits the following corrective action plan for the year ended June 30, 2004.

Name and address of independent public accounting firm: Juan Rivera, CPA, G-23, Mireya St., Boulevard Ave., Levittown, P.R. 00949

Audit period: Fiscal year ended June 30, 2004

The findings from the June 30, 2004 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

FINDINGS - FEDERAL AWARD PROGRAM AUDITS, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Finding 04-1: Section 8 - CFDA No. 14.855

Reportable Condition: See Condition 04-1

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We observed the 76% of our sample of participants who were selected from the waiting list. The Municipality should improve this procedure in order to comply with at least 98%.

Recommendation

The Municipality should continue with the procedures of selecting from the waiting list in order to give the same opportunity to all participants and to comply with federal regulations.

Action Taken

We are including our improved Waiting List to comply with the 98%, and instructions were given to the Section 8 Coordinator to select participants from this waiting list.

Finding 04-2: Section 8 - CFDA No. 14.855

Reportable Condition: See Condition 04-2

The Municipality should implement the reasonable written method established in the Administrative Plan to determine and document for each unit leased that the rent to owner is reasonable based on current rents for comparable unassisted units.



Recommendation

The Municipality should implement as soon as possible the complete reasonable method written in the Administrative Plan in order to comply with federal regulations.

Action Taken

The Municipality is including reasonable written method which was done taking an example in some of the Camuy Wards, and instructions were given to the Section 8 Coordinator to enforce this method immediately.

Finding 04-3: Section 8 - CFDA No. 14.855

Reportable Condition: See Condition 04-3

During the audit we can observe the procedures of housing quality standards (HQS) are implemented and the deficiencies are corrected into time required, but the procedures should be improved because some deficiencies are not corrected yet in some cases.

Recommendation

The Municipality should improve more the HQS procedures in order to comply with federal regulations.



Action Taken

We are including table of inspection dates for the housing units, and instructions were given to the Section 8 Coordinator to correct this situation as soon as possible.

Finding 04-4: SBGP – CFDA N o. 14.228

Reportable Condition: See Condition 04-4

During the audit we observed there are some construction projects that require complying with Davis-Bacon Act. The Federal Programs Office did not realize the procedures of interviews and payroll reviews.

Recommendation

The Municipality should assign these duties to a federal programs employee in order to comply with federal regulations.

Action Taken

Instructions were given to the Programs Inspector to realize the interview to the employees of the Contractors in order to correct this situation as soon as possible.



Finding 04-5: SBGP - CFDA No. 228

Reportable Condition: See Condition 04-5

The Federal Programs Office does not maintain a physical inventory of the equipment acquired by federal funds.

Recommendation

The Municipality should implement a physical inventory and maintain it in the Federal Programs Offices in order to comply with federal regulations.

Action Taken

The Municipality is enclosing a physical inventory of equipment belonging to the Federal Programs Office, and instructions were given to the Accountant in order to maintain this record.

Finding 04-6: SBGP - CFDA No. 14.228

Reportable Condition: See Condition 04-6

The SBGP program should minimize the time elapsing between transfer the federal funds from agency (OCAM) and disbursement to suppliers.



Recommendation

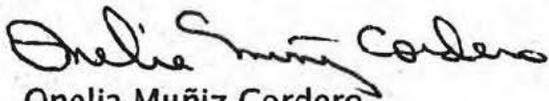
The Municipality should establish procedures in conjunction with the Finance Department in order to make the disbursement into the time required.

Action Taken

Instructions were given to the Accountant to correct this situations as soon as possible.

If the Cognizant or Oversight Agency for Audit has questions regarding this plan, please call Mrs. Onelia Muñiz Cordero at (787) 262-7704.

Sincerely yours,


Onelia Muñiz Cordero
Federal Programs Director