

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

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

Candela Jr 9862

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY
SINGLE AUDIT REPORT
YEAR ENDED JUNE 30, 2004

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2004

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2004

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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

INDEPENDENT AUDITORS' REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Cayey
Cayey, 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 Cayey, Puerto Rico**, as of and for the year ended June 30, 2004, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

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 Cayey, 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.

The Management's Discussion and Analysis on pages 3 through 11 and the Budgetary Comparison Schedule-General Fund on page 38 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

INDEPENDENT AUDITORS' REPORT (Continued)

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2004 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 20, 2004

Stamp No.2019436 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2004

Management's Discussion and Analysis

As management of the Municipality of Cayey, we offer readers of the Municipality's basic financial statements this narrative overview and analysis of the financial activities of the Municipality as of and for the fiscal year ended June 30, 2004. This Management's Discussion and Analysis (MD&A) include comparative data, and it has been designed accordingly with the following goals:

- a) Assist the reader in focusing on significant financial issues,
- b) Provide an overview of the Municipality's financial activity,
- c) Identify changes in the Municipality's financial position (its ability to address the next and subsequent year challenges),
- d) Identify any material deviations from the financial plan (the approved budget,) and;
- e) Identify individual fund issues or concerns.

Since the MD&A is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the Municipality's financial statements.

FINANCIAL HIGHLIGHTS

- The Municipality net assets increase by \$ 20,226,302.
- In the fund financial statements, the governmental activities revenue increase \$ 15,891,284 (or 54%) while governmental activities expenditures increase \$ 12,166,948 (or 37%).
- The General Fund (the primary operating fund) reflected, on a current financial resource basis, a decrease of \$ 190,470.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$ 685,164.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Using This Annual Report

This annual report consists of a series of new financial statements with a change in the focus from 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.

Government-Wide Financial Statements

The Government-Wide Financial Statements are designed to provide users of the financial statements with a broad overview of the Municipality's finances in a manner similar to private-sector companies.

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

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the Statement of Activities that will only result in cash flows in future fiscal periods. The Statement of Activities is focused on both the gross and net cost of various activities, which are provided by the government's general tax and other revenues. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

Fund Financial Statements

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements, focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Fund Financial Statements (Continued)

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

Infrastructure Assets

Historically, a government's largest group of assets (infrastructure-roads, bridges, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the Governmental column of the Government-Wide 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 (the modified approach) which periodically (at least every third year), by category, measures and demonstrated 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.

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 a government's financial position. The Municipality's combined net assets (excess of assets over liabilities) totaled \$ 35,695,428 at the end of 2004, compared to \$ 15,469,126 at the end of the previous year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

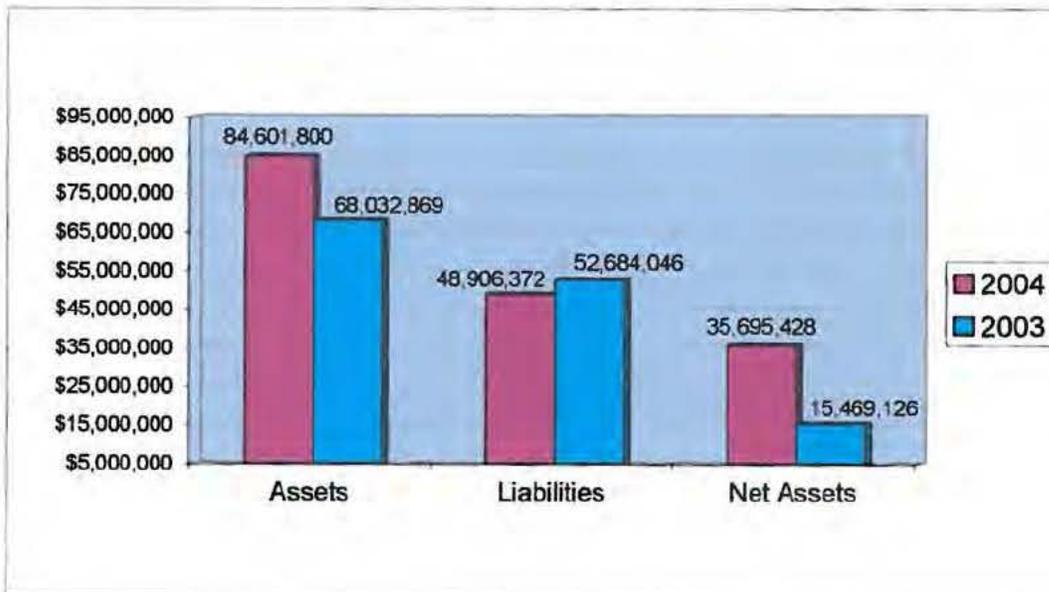
MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2004

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets (Continued)

Condensed Statement of Net Assets	2004	2003	Change	%
Current assets	\$40,847,683	\$27,399,365	\$13,448,318	49%
Capital assets	23,143,895	20,356,710	2,787,185	14%
Other assets	20,610,222	20,276,794	333,428	2%
Total assets	84,601,800	68,032,869	16,568,931	24%
Current liabilities	8,448,386	10,601,497	(2,153,111)	(20%)
Noncurrent liabilities	40,457,986	42,082,549	(1,624,563)	(4%)
Total liabilities	48,906,372	52,684,046	(3,777,674)	(7%)
Invested in capital assets, net of related debt	16,057,117	12,085,504	3,971,613	33%
Restricted	30,936,243	15,144,344	15,791,899	104%
Unrestricted	(11,297,932)	(11,760,722)	462,790	(4%)
Total net assets	\$35,695,428	\$15,469,126	\$20,226,302	131%



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Changes in Net Assets

The Municipality's net assets increase by \$20,226,302. Approximately 38 percent of the Municipality's total revenue came from taxes, while 56 percent resulted from grants and contributions, including federal aid. Charges for Services provided 4 percent and Interest revenue and miscellaneous 2 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for health and welfare services, general government, public works, and public safety. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

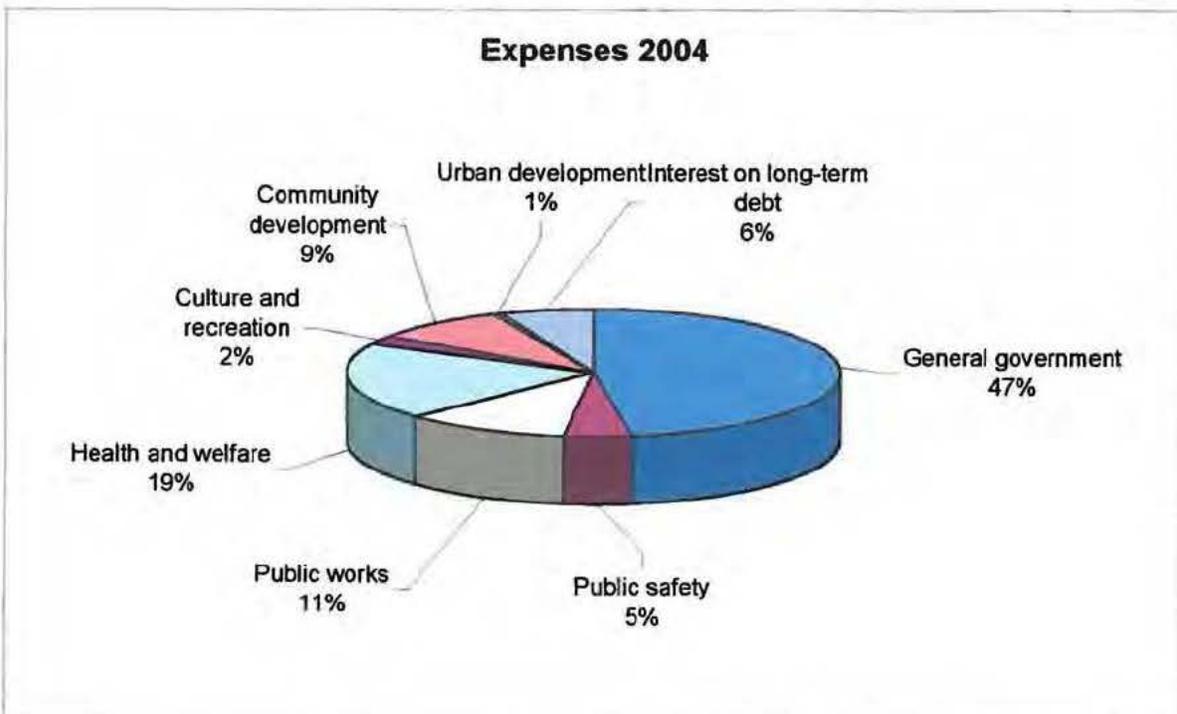
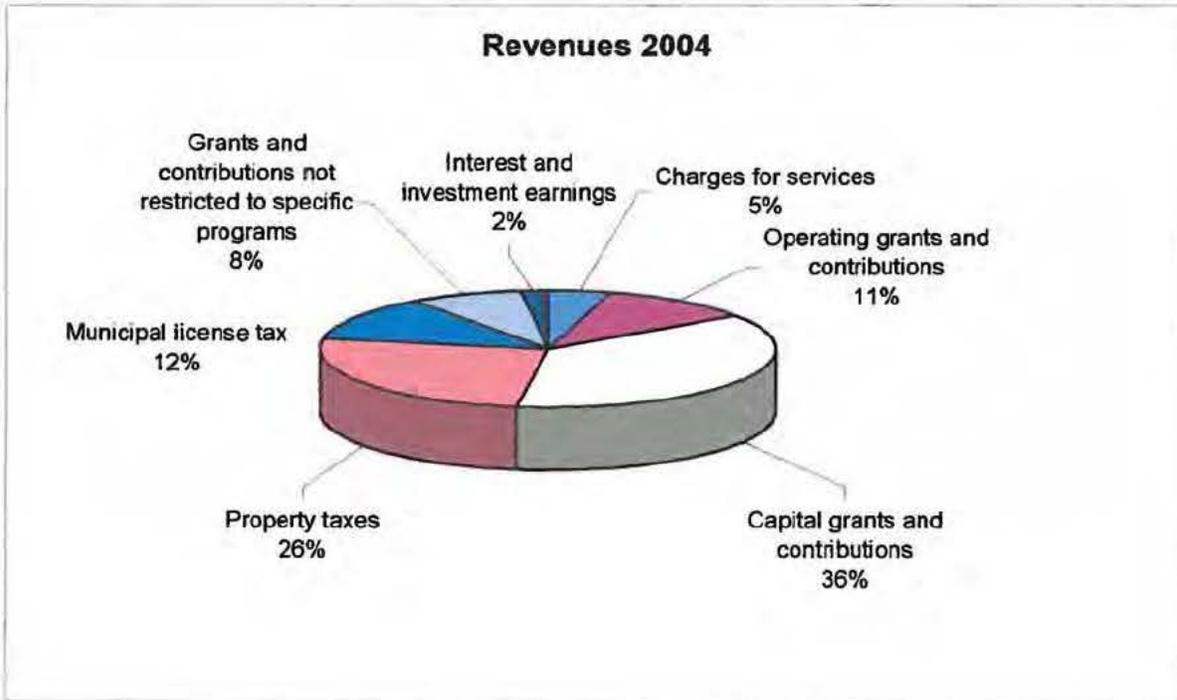
Condensed Statement of Activities	2004	2003	Change	%
Program revenues:				
Charges for services	\$2,049,438	\$2,019,292	\$30,146	1%
Operating grants and contributions	4,879,383	4,765,472	113,911	2%
Capital grants and contributions	16,818,205	2,822,912	13,995,293	496%
General revenues:				
Property taxes	11,690,960	10,777,185	913,775	8%
Municipal license tax	5,505,096	4,463,014	1,042,082	23%
Grants and contributions not restricted to specific programs	3,631,358	4,224,590	(593,232)	(14%)
Interest and investment earnings	779,504	365,764	413,740	113%
Miscellaneous	135,243	227,609	(92,366)	(41%)
Total revenues	45,489,187	29,665,838	15,823,349	53%
Expenses:				
General government	11,228,349	12,167,758	(939,409)	(8%)
Public safety	1,089,662	850,239	239,423	28%
Public works	2,536,207	14,640,706	(12,104,499)	(83%)
Health and welfare	4,606,321	4,977,747	(371,426)	(7%)
Culture and recreation	584,066	773,353	(189,287)	(24%)
Community development	2,082,079	432,290	1,649,789	382%
Urban development	119,049		119,049	100%
Interest on long-term debt	1,453,643	652,683	800,960	123%
Education	1,563,509	146,577	1,416,932	967%
Total expenses	25,262,885	34,641,353	(9,378,468)	(27%)
Change in net assets	20,226,302	(4,975,515)	25,201,817	(507%)
Net assets, beginning of year	15,469,126	20,444,641	(4,975,515)	(24%)
Net assets, end of year	\$35,695,428	\$15,469,126	\$20,226,302	131%

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2004

Changes in Net Assets (Continued)



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

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

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$32,399,297, an increase of \$15,596,661 in comparison with the prior year. There are reservations of fund balance amounting to \$32,382,879. This is the fund balance that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior fiscal year (\$1,446,636), 2) to pay debt service (\$ 4,796,803), 3) to pay for capital projects (\$20,503,408) and 4) for other purposes (\$ 5,636,032).

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2004, the general fund has a fund balance of \$ 1,463,054.

GENERAL FUND BUDGETARY HIGHLIGHTS

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

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2004, amounts to \$ 64,595,319, net of accumulated depreciation of \$ 20,841,201, leaving a net book value of \$ 43,754,119. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure and construction in progress. Infrastructure

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2004

CAPITAL ASSETS AND DEBT ADMINISTRATION- (CONTINUED)

assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The total increase in the Municipality's investment in capital assets for the current fiscal year was about 8% in terms of net book value. Depreciation charges for the year totaled \$ 4,347,169.

The Municipality finances a significant portion of its construction activities through bond issuances. 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. As of June 30, 2004, the Municipality has \$20,503,408 of unexpended proceeds mainly from bond issuances that are committed to future construction activities.

Debt Administration

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged. See "Limitations on Ability of Municipalities to Issue General Obligation Debt-The Municipal Bonds" for a general description of such limitations.

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

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation,

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

CAPITAL ASSETS AND DEBT ADMINISTRATION- (CONTINUED)

municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal grant revenues may vary if new grants are available but the revenue also is very predictable.

Those factors were considered when preparing the Municipality's budget for the 2004-2005 fiscal year.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer.

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

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 28,440,554
Cash with fiscal agent	11,113,919
Accounts receivable:	
Municipal license tax	2,998
Federal grants	766,520
Other	637
Notes receivable	523,055
Capital assets	
Land, improvements, and construction in progress	23,143,895
Other capital assets, net of depreciation	20,610,222
Total capital assets	<u>43,754,117</u>
 Total assets	 <u>84,601,800</u>
 Liabilities	
Accounts payable and accrued liabilities	1,736,362
Due to other governmental entities	370,535
Deferred revenues:	
Municipal license tax	4,221,792
Federal grant revenues	2,119,697
Noncurrent liabilities:	
Due within one year	3,735,990
Due in more than one year	<u>36,721,996</u>
 Total liabilities	 <u>48,906,372</u>
 Net Assets	
Invested in capital assets, net of related debt	16,057,117
Restricted for:	
Capital projects	20,503,408
Debt service	4,796,803
Federal and state grant funds	5,636,032
Unrestricted (deficit)	<u>(11,297,932)</u>
 Total net assets	 <u>\$ 35,695,428</u>

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

Commonwealth of Puerto Rico
Municipality of Cayey
Statement of Activities
For the Year Ended June 30, 2004

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes In Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 11,228,349	\$ 85,567	\$ 445,207	\$ -	\$ (10,697,575)
Public safety	1,089,662	39,040	55,529		(995,093)
Public works	2,536,207	233,134	308,257	16,366,559	14,371,743
Health and welfare	4,606,321	1,674,697	1,359,904		(1,571,720)
Culture and recreation	584,066	17,000	2,598		(564,468)
Community development	2,082,079		1,799,842	332,597	50,360
Urban development	119,049			119,049	-
Interest on long-term debt	1,453,643				(1,453,643)
Education	1,563,509		908,046		(655,463)
Total governmental activities	\$ 25,262,885	\$ 2,049,438	\$ 4,879,383	\$ 16,818,205	(1,515,859)

General revenues:

Property taxes	11,690,960
Municipal license tax	5,505,096
Grants and contributions not restricted to specific programs	3,631,358
Interest and investment earnings	779,504
Miscellaneous	135,243

Total general revenues

21,742,161

Change in net assets

20,226,302

Net assets - beginning as restated

15,469,126

Net assets - ending

\$ 35,695,428

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

	<u>General Fund</u>	<u>Special Revenue Fund - State & Federal Grants</u>	<u>Capital Projects Fund - State & Federal Grants</u>	<u>Debt Service Fund</u>	<u>Total Governmental Funds</u>
Assets					
Cash and cash equivalents	\$ 6,601,269	\$ 3,513,542	\$ 18,325,743	\$ -	\$ 28,440,554
Cash with fiscal agent		2,817,575	3,499,541	4,796,803	11,113,919
Accounts receivable:					
Municipal license tax	2,998				2,998
Federal grants		546,842	219,678		766,520
Other		637			637
Due from other funds	180,530	6,046	431,336		617,912
Notes receivable			523,055		523,055
Total assets	<u>\$ 6,784,797</u>	<u>\$ 6,884,642</u>	<u>\$ 22,999,353</u>	<u>\$ 4,796,803</u>	<u>\$ 41,465,595</u>
Liabilities and Fund Balances					
Liabilities :					
Accounts payable and accrued liabilities	\$ 593,673	\$ 423,315	\$ 719,374	\$ -	\$ 1,736,362
Due to other governmental entities	370,535				370,535
Due to other funds	135,743	481,924	245		617,912
Deferred revenues:					
Municipal license tax	4,221,792				4,221,792
Federal grant revenues		343,371	1,776,326		2,119,697
Total liabilities	<u>5,321,743</u>	<u>1,248,610</u>	<u>2,495,945</u>	<u>-</u>	<u>9,066,298</u>
Fund balances:					
Reserved for:					
Encumbrances	1,446,636				1,446,636
Capital projects			20,503,408		20,503,408
Other purposes		5,636,032			5,636,032
Debt service fund				4,796,803	4,796,803
Unreserved:					
Undesigned	16,418				16,418
Total fund balances	<u>1,463,054</u>	<u>5,636,032</u>	<u>20,503,408</u>	<u>4,796,803</u>	<u>32,399,297</u>
Total liabilities and fund balances	<u>\$ 6,784,797</u>	<u>\$ 6,884,642</u>	<u>\$ 22,999,353</u>	<u>\$ 4,796,803</u>	

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

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	43,754,117
Long-term liabilities are not due and payable in the current period, and therefore, are not reported in the funds	<u>(40,457,986)</u>
Net assets of governmental activities	<u>\$ 35,695,428</u>

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

	General Fund	Special Revenue Fund - State & Federal Grants	Capital Projects Fund - State & Federal Grants	Debt Service Fund	Total Governmental Funds
Revenues					
Property taxes	\$ 7,892,490	\$ -	\$ -	\$ 3,214,204	\$ 11,106,694
Municipal license taxes	5,505,096				5,505,096
Licenses, permits and other local taxes	2,166,853				2,166,853
Charges for services	1,918,324				1,918,324
Intergovernmental	2,180,767	1,766,901	16,146,902		20,094,570
Fines and forfeitures	5,611				5,611
Interest	779,504				779,504
Federal grants		2,989,494	671,303		3,660,797
Miscellaneous	113,303	85,988	79		199,370
Total revenues	20,561,948	4,842,383	16,818,284	3,214,204	45,436,819
Expenditures					
Current:					
General government	10,783,835	406,491	134		11,190,460
Public safety	1,313,316	72,227			1,385,543
Public works	3,167,036	979,667	2,164,767		6,311,470
Health and welfare	3,548,441	1,345,189			4,893,630
Culture and recreation	780,727	1,666			782,393
Community development	299,230	637,704	332,597		1,269,531
Education	191,087	1,376,607			1,567,694
Urban Development			119,049		119,049
Debt service:					
Principal		675,000		1,691,000	2,366,000
Interest		434,770		1,018,873	1,453,643
Total expenditures	20,083,672	5,929,321	2,616,547	2,709,873	31,339,413
Excess (deficiency) of revenues over (under) expenditures	478,276	(1,086,938)	14,201,737	504,331	14,097,406
Other financing sources (uses)					
Transfers in	93,870	153,015	614,369		861,254
Transfers out	(762,616)	(93,870)	(4,768)		(861,254)
Long-term debt issued		1,515,000			1,515,000
Bond issuance costs		(15,745)			(15,745)
Total other financing sources (uses)	(668,746)	1,558,400	609,601	-	1,499,255
Net change in fund balances	(190,470)	471,462	14,811,338	504,331	15,596,661
Fund balance, beginning as restated	1,653,524	5,164,570	5,692,070	4,292,472	16,802,636
Fund balance, ending	\$ 1,463,054	\$ 5,636,032	\$ 20,503,408	\$ 4,796,803	\$ 32,399,297

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

Commonwealth of Puerto Rico
Municipality of Cayey
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2004

Net Change in Fund Balances - Total Governmental Funds \$ 15,596,661

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period. 8,527,663

Depreciation expense on capital assets is reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds (4,347,169)

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in Governmental Funds. (1,418,161)

Some revenues reported in the Statement of Activities do not provide current financial resources in Governmental Funds. 52,368

Change in landfill accrual 948,195

The issuance of long-term debt provides current financial resources to Governmental Funds, while the repayment of principal of long-term debt consumes current financial resources. This is the amount by which debt service principal payments exceed debt proceeds. 866,745

Change in Net Assets of Governmental Activities \$ 20,226,302

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Cayey** (the Municipality) was founded on the year 1773. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a sixteen-member Municipal Legislature who are elected for four-year terms.

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

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

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

As part of this Statement, there is a new reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). The Municipality has applied the retroactively presentation of the historical costs of infrastructure assets during the fiscal year ended June 30, 2003.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

A. Component Units

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

B. Government-wide and fund financial statements

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

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

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenue. Direct expenses are those that are charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

B. Government-wide and fund financial statements

a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

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

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

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

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

C. Financial reporting presentation

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

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

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

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

Capital Projects Funds- Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

D. Measurement focus, basis of accounting and financial presentation

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

D. Measurement focus, basis of accounting and financial presentation

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

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

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

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

E. Assets, liabilities and net assets

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

Cash with fiscal agent in the debt services fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law.

- 2. Receivables and payables-** Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivable in the special revenue fund represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs and the amount in the debt service fund represent the distribution of property tax collected by the Municipal Revenue Collection Center (CRIM), which is restricted for the debt service.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

E. Assets, liabilities and net assets

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

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

Capital assets of the Municipality, as well as the component unit, are depreciated using the straight-line method over the following estimated useful lives:

Description	Useful Life	Capitalization threshold
Buildings	50	\$ 1
Infrastructure (roads)	20	\$ 1
Machinery	10	\$ 25
Computer's hardware	5	\$ 25
Vehicles	5	\$ 1
Furniture and fixtures	10	\$ 25
Stadiums	20 to 45	\$ 1
Recreational areas	10 to 15	\$ 1

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

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

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

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

E. Assets, liabilities and net assets

7. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.
8. **Reservation of fund balance-** Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The municipality has the following reservations of fund balance:
 - a. *Capital Projects-* Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
 - b. *Encumbrances-* Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
 - c. *Debt Service Fund-* Represents net assets available to finance future debt service payments.
 - d. *Other Purposes-* Represents net assets available for specific use and/or legally segregated for other specific future use.
9. **Interfund and intra-entity transactions-** The Municipality has the following types of transactions among funds:
 - a. *Operating Transfers-* Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
 - b. *Intra-Entity Transactions-* Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
10. **Risk financing-** The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

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

E. Assets, liabilities and net assets

gross property tax collections by the CRIM for the year ended June 30, 2004 amounted to approximately \$ 470,000. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$ 383,000 for workers compensation insurance covering all municipal employees.

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

		<u>Total Net Assets - Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 43,754,117	
Deduct:		
Bonds Payable	(22,072,000)	
Notes Payable	<u>(5,625,000)</u>	\$16,057,117
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		20,503,408
<u>Net assets restricted for debt service</u>		
Fund balance restricted for debt service		4,796,803
<u>Net assets restricted for other purposes</u>		
Fund balance restricted for other purposes		5,636,032
<u>Net assets unrestricted (deficit)</u>		
General fund - total fund balance:	\$ 1,463,054	
Deduct:		
Compensated absences	(2,373,974)	
Landfill obligation	(4,015,719)	
Advances from CRIM	(5,029,385)	
Claims and judgments debt	(50,000)	
Due to other governmental entity	<u>(1,291,908)</u>	<u>(11,297,932)</u>
Total net assets - governmental activities		<u>\$ 35,695,428</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

2. DEPOSITS

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

The Municipality's bank balances in commercial banks of approximately \$ 6,600,000 in the general fund were fully collateralized at June 30, 2004. In the special revenue and capital projects funds there were deposits with commercial banks of approximately \$ 3,500,000 and \$ 18,300,000 respectively, that were fully collateralized.

The deposits at GDB of approximately \$ 3,500,000 that are restricted principally for capital projects, \$ 2,800,000 that are restricted for various purposes and the \$ 4,796,803 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

- a. **Municipal License Tax**- The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$ 1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2004, the tax rates were as follows:

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

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2004, net of allowance for uncollectibles. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

- b. **Federal Grants**- Federal Grants receivable in the special revenue and capital projects funds mainly consist in expenditures incurred not yet reimbursed by the CDBG Program.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

4. NOTES RECEIVABLE

At June 30, 2004, the notes receivable are composed of the following:

a. Note receivable from Cooperativa Agro-Comercial de P.R. " La Marquetin" in the original amount of \$ 740,000, to be collected as follows:	\$ 360,197
1. Monthly interest payments of \$ 1,850, at 3 % annual interest rate, from the first through the end of the fifth year.	
2. Monthly installments of \$ 5,110 including interest at 3 %, starting on the sixth year through year 2011.	
b. Note receivable from Hospital Menonita in the original amount of \$350,000 to be collected in monthly installments of \$3,037, including interest at 8.5% through year 2012.	<u>162,858</u>
Total amount of notes receivable as of June 30, 2004	<u>\$ 523,055</u>

5. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2004 are summarized as follows:

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Special Revenue Fund (70)	\$ 38,268
	Special Revenue Fund (02)	142,017
	Capital Projects Fund	245
Special Revenue	General Fund	6,037
	Special Revenue Fund (70)	9
Capital Projects	General Fund	129,706
	Special Revenue Fund (70)	<u>361,630</u>
Total		<u>\$ 617,912</u>

b. Transfer in/out to other fund

Following is a summary of interfund transfers for the year:

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund	Various	\$ 148,247
Special Revenue	General Fund	Various	93,870
General Fund	Capital Projects	Transfer of funds for capital outlays	614,369
Capital Projects	Special Revenue Fund	Reclassification of cash balance	<u>4,768</u>
Total			<u>\$ 861,254</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

6. CAPITAL ASSETS

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2004, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

Governmental Activities:	Balance July 1, 2003	Additions	Retirements	Balance June 30, 2004
Capital asset, not being depreciated:				
Land	\$ 17,991,546	\$ 362,707	\$ —	\$18,354,253
Construction in progress	2,365,164	3,536,726	(1,112,247)	4,789,643
Total capital assets not being depreciated	20,356,710	3,899,433	(1,112,247)	\$23,143,895
Capital assets, being depreciated:				
Buildings and building improvements	23,744,293	1,253,899	—	24,998,192
Equipment	1,402,415	1,212,457	—	2,614,872
Infrastructure	5,326,724	831,242	—	6,157,966
Vehicles	6,297,394	1,382,999	—	7,680,393
Total capital assets being depreciated	\$ 36,770,826	\$ 4,680,597	\$ —	41,451,423
Less accumulated depreciation for:				
Buildings and building improvements	(8,873,938)	(2,656,859)	—	(11,530,797)
Equipment	(585,928)	(153,407)	—	(739,335)
Infrastructure	(4,013,989)	(1,326,396)	—	(5,340,385)
Vehicles	(3,020,177)	(210,507)	—	(3,230,684)
Total accumulated depreciation	(16,494,032)	(4,347,169)	—	(20,841,201)
Total capital assets being depreciated, net	20,276,794	333,428	—	20,610,222
Governmental activities capital assets, net	\$ 40,633,504	\$ 4,232,862	(\$ 1,112,247)	\$ 43,754,117

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

6. CAPITAL ASSETS (CONTINUED):

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

Governmental activities:

General government	\$714,614
Public safety	11,756
Public works	1,411,167
Community development	2,016,954
Culture and recreation	40,687
Health and welfare	151,154
Education	<u>837</u>
Total depreciation expense-governmental activities	<u>\$ 4,347,169</u>

7. PROPERTY TAXES

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

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

7. PROPERTY TAXES (CONTINUED):

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

The annual tax rate is 8.83% for real property and 6.83% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 2.00% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund. The Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected and such amount is accounted for similar to item (a) above.

8. DUE TO OTHER GOVERNMENTAL ENTITIES:

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

General Services Administration	\$ 1,409
Puerto Rico Telephone Company	42,866
Puerto Rico Aqueduct and Sewer Authority	8,864
Puerto Rico Electric Power Authority	<u>317,396</u>
Total	<u>\$ 370,535</u>

The Municipality reached agreements with other governmental entities for the payment of debts on a long-term basis. These liabilities are presented in the Statement of Net Assets as non-current liabilities.

9. DEFERRED REVENUES

- a. **Municipal License Tax-** The deferred revenues of approximately \$4,200,000 in the general fund relates to municipal license tax collected in fiscal year 2003-04 that will be earned in fiscal year 2004-05.
- b. **Federal Government-** The deferred revenues presented in Special Revenue and Capital Projects Funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

9. DEFERRED REVENUES (CONTINUED):

Program Description

HUD- Section 108	\$ 1,477,135
Section 8 Housing Choice Vouchers	253,661
Local Law Enforcement Block Grants	32,422
Public Assistance Grant (FEMA)	238,123
Other	<u>118,356</u>
 Total	 <u>\$ 2,119,697</u>

10. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2004, was as follows:

	Beginning Balance	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds Payable	\$22,248,000	\$1,515,000	\$(1,691,000)	\$22,072,000	\$1,957,000
Notes Payable	6,300,000		(675,000)	5,625,000	675,000
Advances from CRIM	4,880,712	535,004	(386,331)	5,029,385	933,990
Compensated Absences	2,155,921	218,053		2,373,974	170,000
Due to other Governmental entity	1,352,720		(60,812)	1,291,908	
Claims and Judgments	181,282		(131,282)	50,000	
Landfill obligation	4,963,914		(948,195)	4,015,719	
Total	<u>\$42,082,549</u>	<u>\$2,268,057</u>	<u>\$(3,892,620)</u>	<u>\$40,457,986</u>	<u>\$3,735,990</u>

- a. **Legal debt margin-** The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment if property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues if the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds payable, is paid with unrestricted funds.
- b. **Bonds payable-** The Municipality issues general and special obligation bonds to provide funds for the acquisition of equipment and construction of major capital facilities. During the current year, the Municipality issued bonds for approximately \$1,515,000. Bonds payable outstanding at June 30, 2004 are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

10. LONG-TERM LIABILITIES (CONTINUED)

Type of bonds	Maturity date	Original Amount	Range of Interest rates	Balance at June 30, 2004
1989 Series	7-1-04	460,000	3.3% to 8.6%	\$ 55,000
1992 Series	7-1-07	2,440,000	4.2% to 6.4%	1,000,000
1995 Series	1-1-18	663,000	5.0%	487,000
1995 Series	1-1-18	465,000	5.0%	335,000
1997 Series	7-1-07	280,000	6.0% to 7.5%	140,000
1998 Series	7-1-22	1,015,000	4.9% to 6.7%	915,000
1998 Series	7-1-13	1,990,000	4.9% to 6.7%	1,495,000
1998 Series	7-1-13	355,000	4.9% to 6.7%	275,000
1998 Series	7-1-13	3,705,000	4.9% to 6.7%	2,885,000
1999 Series	7-1-05	355,000	0.0% to 7.8%	120,000
1999 Series	7-1-12	725,000	6.0% to 7.1%	545,000
1999 Series	7-1-23	685,000	6.0% to 7.0%	625,000
2000 Series	7-1-04	55,000	7.3% to 7.5%	15,000
2000 Series	7-1-04	250,000	0.0% to 7.8%	55,000
2000 Series	7-1-06	355,000	7.3% to 7.5%	320,000
2000 Series	7-1-14	1,765,000	7.3% to 7.5%	1,460,000
2001 Series	7-1-05	180,000	5.0% to 8.0%	80,000
2001 Series	7-1-25	270,000	5.0% to 8.0%	255,000
2001 Series	7-1-25	1,010,000	5.0% to 8.0%	965,000
2001 Series	7-1-06	165,000	5.0% to 7.5%	110,000
2001 Series	7-1-16	255,000	5.0% to 8.0%	235,000
2001 Series	7-1-08	325,000	5.0% to 7.5%	250,000
2001 Series	7-1-06	475,000	5.0% to 7.5%	305,000
2001 Series	7-1-16	1,120,000	5.0% to 7.5%	1,030,000
2001 Series	7-1-18	835,000	5.0% to 7.5%	780,000
2002 Series	7-1-06	260,000	5.0% to 8.0%	165,000
2002 Series	7-1-16	125,000	5.0% to 7.5%	115,000
2002 Series	7-1-08	205,000	5.0% to 7.5%	155,000
2002 Series	7-1-26	255,000	5.0% to 7.25%	245,000
2002 Series	7-1-07	55,000	5.0% to 6.5%	45,000
2002 Series	7-1-08	205,000	5.0% to 6.5%	200,000
2002 Series	7-1-17	235,000	5.0% to 6.5%	225,000
2002 Series	7-1-07	270,000	5.0% to 6.5%	225,000
2002 Series	7-1-17	325,000	5.0% to 6.5%	310,000
2002 Series	7-1-09	1,030,000	5.0% to 6.5%	910,000
2004 Series	7-1-09	745,000	5.0% to 6.5%	660,000
2004 Series	7-1-17	85,000	2.7% to 5.0%	80,000
2004 Series	7-1-27	1,110,000	5.0% to 6.5%	1,095,000
2004 Series	7-1-27	1,415,000	5.0% to 6.5%	1,390,000
2004 Series	7-1-13	120,000	5.0% to 6.0%	120,000
2004 Series	7-1-28	140,000	2.36% to 6.0%	140,000
2004 Series	7-1-10	180,000	5.0% to 6.0%	180,000
2004 Series	7-1-18	205,000	2.36% to 4.0%	205,000
2004 Series	7-1-08	265,000	2.36% to 6.0%	265,000
2004 Series	7-1-08	605,000	5.0% to 6.0%	605,000

Total general obligation bonds

\$ 22,072,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

10. LONG-TERM LIABILITIES (CONTINUED):

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

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

Year Ending June 30,	Principal	Interest
2005	\$ 1,957,000	\$ 1,199,653
2006	1,954,000	1,129,174
2007	1,996,000	1,024,897
2008	1,924,000	923,897
2009	1,616,000	828,693
2010-2014	6,646,000	2,776,370
2015-2019	3,084,000	1,279,550
2020-2024	1,810,000	614,446
2025-2029	1,085,000	128,725
Total	<u>\$ 22,072,000</u>	<u>\$ 9,905,405</u>

- c. **Advances from CRIM-** This amount represents the balance owed to CRIM at June 30, 2004 will be repaid through a financing obtained by the CRIM with GDB.
- d. **Compensated absences-** The government-wide statement of net assets includes approximately \$ 2,400,000 of accrued vacation and sick leave benefits, representing the Municipality's commitment to fund such costs from future operations.
- e. **Landfill obligation-** State and federal laws and regulations require the Municipality to place a final cover on its landfill site, when it stopped accepting waste, and perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with Statement No. 18 of the GASB, "Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs", the Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Based on this study, the Municipality has recognized \$ 4,015,719 as the Municipality's estimated current cost for landfill closure and post-closure costs as of June 30, 2004. The annual estimate of post closure costs has been assessed approximately to be \$ 47,000 for a period of approximately 30 years. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. The balance of closure and post-closure costs are reported in the government-wide statement of net assets.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

10. LONG-TERM LIABILITIES (CONTINUED):

- f. **Notes payable-** The notes payable transactions for the year ended June 30, 2004, were as follows:

Balance at July 1, 2003	\$ 6,300,000
Payment during the current year	<u>(675,000)</u>
Balance at June 30, 2004	<u>\$ 5,625,000</u>

Notes payable at June 30, 2004 are as follows:

Description	Maturity Date	Original Amount	Range of Interest rates	Balance June 30, 2004
Section 108 Loan	8-1-06	\$ 3,330,000	5.9% to 7.1%	\$ 1,230,000
Section 108 Loan	8-1-14	1,670,000	6.2% to 6.5%	1,230,000
Section 108 Loan	8-1-15	4,225,000	6.2% to 6.5%	<u>3,165,000</u>
				<u>\$ 5,625,000</u>

The future annual requirements for the amortization of notes payable outstanding as of June 30, 2004, are as follows:

<u>Year ending June 30,</u>	<u>Amount</u>
2005	675,000
2006	1,025,000
2007	655,000
2008	375,000
2009	375,000
2010-2014	1,875,000
2015-2018	<u>645,000</u>
Total	<u>\$ 5,625,000</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

11. PENSION PLAN

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

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

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

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

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

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions to the above-mentioned plans during the year ended June 30, 2004 recorded as pension expenditures were approximately \$ 423,000. This amount represents 100% of the required contribution for the fiscal year ended June 30, 2004.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

11. PENSION PLAN (CONTINUED)

System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

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

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2004, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940

12. COMMITMENTS AND CONTINGENCIES

A. Federal grants:

The Municipality participates in a number of Federal Financial Assistance Programs. Although the Municipality's grant programs have been audited in accordance with the provisions of the Single Audit Act of 1996, through June 30, 2004, these programs are still subject to financial and compliance audits by the granting agencies and the resolution of previously identified questioned costs. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although the Municipality expects such amounts, if any, not to be material.

B. Claims and lawsuits:

The Municipality is a defendant in several legal proceedings that arise in the ordinary course of the Municipality's activities. With respect to pending and threatened litigation, the Municipality has reported liabilities of \$ 50,000 as non-current liabilities in the Statement of Net Assets of the Government-Wide Financial Statements for anticipated unfavorable judgments. This amount was included in the

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

12. COMMITMENTS AND CONTINGENCIES (CONTINUED)

financial statements and represents the amount estimated as a probable liability or a liability with fixed or expected due date, which will require future available financial resources for its payment.

It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial condition of the Municipality.

13. BEGINNING FUND BALANCES RESTATEMENT:

The beginning fund balance of the Capital Projects Fund has been restated by \$4,768 to properly present the previously reported fund balance as of June 30, 2003.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts (Budgetary Basis) (See Note 1)</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES:				
Property taxes	\$8,099,213	\$ 7,816,694	\$ 7,892,490	\$ 75,796
Municipal license tax	4,750,000	4,830,000	5,505,096	675,096
Licenses, permits and other local taxes	2,575,300	2,595,300	2,166,853	(428,447)
Intergovernmental	2,100,315	2,382,834	2,180,767	(202,067)
Charges for services	2,918,856	3,042,356	1,918,324	(1,124,032)
Fines and forfeitures	20,000	20,000	5,611	(14,389)
Interest	400,000	410,000	779,504	369,504
Miscellaneous	468,500	235,000	113,303	(121,697)
Budgeted carryover		<u>841,914</u>	<u>841,914</u>	<u>-</u>
Total revenues and budget carryover	<u>21,332,184</u>	<u>22,174,098</u>	<u>21,403,862</u>	<u>(770,236)</u>
EXPENDITURES AND ENCUMBRANCES				
Current:				
General government	11,294,737	11,501,651	10,877,587	624,064
Public safety	1,574,086	1,584,086	1,334,787	249,299
Public works	3,393,616	3,643,616	3,420,581	223,035
Culture and recreation	821,609	871,609	832,078	39,531
Health and welfare	3,662,633	3,937,633	3,763,348	174,285
Community development	447,809	447,809	299,230	148,579
Education	<u>187,694</u>	<u>187,694</u>	<u>191,087</u>	<u>(3,393)</u>
Total expenditures and encumbrances	<u>21,382,184</u>	<u>22,174,098</u>	<u>20,718,698</u>	<u>1,455,400</u>
EXCESS OF REVENUES AND BUDGET CARRYOVER OVER EXPENDITURES AND ENCUMBRANCES	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 685,164</u>	<u>\$ 685,164</u>
Explanation of Differences:				
Sources/Inflows of resources:				
Actual amounts (budgetary basis)"available for appropriation" from the budgetary comparison schedule				\$ 21,403,862
Differences-budget to GAAP :				
Transfer from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes.				93,870
Budgeted carryover				<u>(841,914)</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 20,655,818</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$ 20,718,698
Differences-budget to GAAP:				
Transfer to other funds are outflows of budgetary resources but are not expenditures for financial reporting purpose				762,616
Prior year encumbrances recorded as current year expenditures for GAAP basis				811,610
Current year encumbrances recorded as expenditures for budgetary purposes				<u>(1,446,636)</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 20,846,288</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2004

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

a. Budgetary Control

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

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

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2004 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2004.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2004

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF AGRICULTURE:			
Direct Programs:			
Rural Housing Preservation Grant	10.433		\$ 1,120
Pass-through the Commonwealth of Puerto Rico – Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	<u>19,769</u>
Total U.S. Department of Agriculture			<u>20,889</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Programs:			
Community Development Block Grants – Entitlement Grants	14.218		1,747,474
Local Economic	14.221		119,049
Community Development Block Grants – Section 108 Loan Guarantee	14.248		332,597
Section 8 Housing Choice Voucher	14.871		<u>930,011</u>
Total U.S. Department of Housing and Urban Development			<u>3,129,131</u>
U.S. DEPARTMENT OF TRANSPORTATION:			
Direct Program:			
Federal Transit – Formula Grants	20.507		<u>91,512</u>
Total U. S. Department of Transportation			<u>91,512</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)
YEAR ENDED JUNE 30, 2004**

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico – Governors Office (Elderly Office): Special Program for the Aging – Title III, Part B – Grants for Supportive Services and Senior Centers	93.044	Not Available	112,062
Pass-through the Commonwealth of Puerto Rico – Administration for Children and Families: Child Care and Development Block Grant	93.575	Not Available	<u>169,652</u>
Total U.S. Department of Health and Human Services			<u>281,714</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 3,523,246</u>

The accompanying notes are an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2004

A. BASIS OF PRESENTATION:

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

B. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue and Capital Projects Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the funds financial statements and expenditures in the Schedule of Expenditures of Federal Awards is as follows:

<u>Description</u>	<u>Special Revenue</u>	<u>Capital Projects</u>	<u>Total</u>
Per Schedule of Expenditures of Federal Awards	\$ 2,980,088	\$ 543,158	\$ 3,523,246
Non federal programs expenditures	<u>2,949,233</u>	<u>2,073,389</u>	<u>5,022,622</u>
Total expenditures in the fund financial statements	<u>\$ 5,929,321</u>	<u>\$ 2,616,547</u>	<u>\$ 8,545,868</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of

• American Institute of
Certified Public Accountants

• Puerto Rico Society of
Certified Public Accountants

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

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

We have audited the basic financial statements of the **Municipality of Cayey** as of and for the year ended June 30, 2004, and have issued our report thereon dated December 20, 2004, which was unqualified. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the **Municipality of Cayey's** basic 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 basic financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Cayey's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting that, in our judgment, could adversely affect **Municipality of Cayey's** ability to record, process, summarize, and report financial data consistent with the assertions of management in the basic financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items **04-01** through **04-02**.

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

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 basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose reportable conditions that are also to be material weaknesses. However, we believe that none of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs is a material weakness. We also noted other matters involving internal control over financial reporting, which we have reported to management of the **Municipality of Cayey** in a separate letter dated December 20, 2004.

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


LÓPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 20, 2004

Stamp No. 2019437 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

• American Institute of
Certified Public Accountants

• Puerto Rico Society of
Certified Public Accountants

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

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

Compliance

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

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB 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 Cayey's** compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the **Municipality of Cayey's** compliance with those requirements.

In our opinion, the **Municipality of Cayey** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2004. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items, 04-03 through 04-08.

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

Internal Control Over Compliance

The management of the **Municipality of Cayey** is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the **Municipality of Cayey's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on 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 Cayey's** ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items **04-03** through **04-08**.

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 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 on 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 material weakness. However, of the reportable conditions described above, we consider items **04-03** through **04-05** and **04-07** to be material weaknesses. We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Cayey** in a separate letter dated March 15, 2005.



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

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



LÓPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
March 15, 2005

Stamp No. 2019438 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2004

Section I – Summary of Auditors’ Results

Financial Statements

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

Federal awards

Internal Control over major programs:		
Material weakness identified?	Yes X	No
Reportable conditions identified not considered to be material weaknesses?	Yes X	None reported

Type of auditors’ report issued on compliance for major programs: **Unqualified**

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes X	No
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Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
14.218	Community Development Block Grants - Entitlement Grants
14.248	Community Development Block Grants - Section 108 Loan Guarantees
14.871	Section 8 Housing Choice Voucher Program

Dollar threshold used to distinguish between Type A and Type B programs	\$300,000
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Auditee qualified as low-risk auditee?	Yes	No X
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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section II – Financial Statements Findings

Finding Reference	04-01
Requirement	Financial Reporting – Accounting Records
Statement of Condition	During our examination of the Municipality's accounting system we noted that it does not summarize the transactions in a formal General Ledger in order to properly record and account for the transactions of all of its Governmental Funds.
Criteria	Chapter VIII, Article 8.010 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain an effective and updated accounting system.
Cause of Condition	The Municipality accounting data is not summarized in the form of a double-entry General Ledger record.
Effect of Condition	The Municipality's accounting system did not provide updated and complete financial information that presents the financial position and the result of operations and the change in fund balances. Such information is necessary to take management decisions.
Recommendation	We recommend to the Municipality Management to implement internal control and procedures in order to maintain a double entry accounting system that contains accurate information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, interfund transactions, etc.
Questioned Costs	None
Management Response and Corrective Action	The Municipality's Finance Department personnel were instructed to strengthen the control and procedures to assure that the accounting system will provide information regarding authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, interfund transactions, etc.

Implementation Date: July 2005

Responsible Person: Mr. Edwin Quiles Rosario
Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section II - Financial Statements Findings

Finding Reference	04-02
Requirement	Expenditures for Goods and Services and Account Payables - Purchasing and Receiving
Statement of Condition	<p>During our examination of the Municipality's disbursement procedures related to the expenditures for goods and services and account payables process, we noted the following situations:</p> <ul style="list-style-type: none">a. Five (5) disbursement vouchers were not available for our audit.b. In three (3) disbursement vouchers the invoice was missing.c. In one (1) disbursement voucher the receiving report was missing.d. In one (1) disbursement voucher the purchase order was issued after the receiving of goods of services.
Criteria	<p>The Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establish in Chapter Four (4) that the Finance Director will be responsible to account and to prepare disbursements through documents duly prepared and certified, including sufficient evidential matter to support the transactions.</p>
Cause of Condition	<p>The Municipality internal control procedures failed to assure that all transactions include all the required documentation.</p>
Effect of Condition	<p>The Municipality is not in compliance with Chapter Four (4) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.</p>
Recommendation	<p>We recommend to the Municipality's Management to improve its internal control and procedures in order to assure that all disbursement vouchers were properly safeguarded, and to assure that any disbursement transaction be properly supported by required documentation.</p>
Questioned Cost	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section II - Financial Statements Findings

Finding Reference **04-02 (continued)**

**Management Response
and Corrective Action** The Municipality's Management instructed Finance Department
personnel in order to strengthen control and procedures to assure that
conditions observed by the auditors does not occur again.

Implementation Date: April 2005

Responsible Person: Mr. Edwin Quiles Rosario
Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-03
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Financial Administration-Standard for Financial Management System
Statement of Condition	During our audit, we noted that the set of accounting records maintained for the fiscal year 2003-2004 did not present properly the financial position and the results of operations of the program.
Criteria	<p>Code of Federal Regulations 24, Subpart C, Part 85.20 (b) (2) states that the grantees and sub grantees must maintain records, which adequately identify the source and application of funds, provided for financially-assisted activities. These records must contain information pertaining to grant or sub grant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.</p> <p>The Voucher Program Guidebook-Housing Choice (7420.10G), Chapter 20, Financial Management, states the financial record keeping and management requirements with respect to Housing Assistance Payments Program Projects under annual contribution contracts.</p>
Cause of Condition	The Municipality maintained a cash basis accounting records for the Program. Also, the General Ledger did not contain some necessary accounts to properly post cash and modified accrual basis transactions.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulation 24, Subpart C, Part 85.20 (b) (2).
Recommendation	We recommended to management to instruct the program accountant to follow financial management and accounting procedures established in the Voucher Program Guidebook-Housing Choice (7420.10G), Chapter 20, Financial Management, and the policies and procedures established in the Low Rent Housing Accounting Guide (7510.1).
Questioned Cost	None.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **04-03 (continued)**

**Management Response
and Corrective Action**

The Municipality's management gave instructions to the program accountant to modify the accounting records in order to comply with the Program financial management and accounting requirements. Also, the Municipality's management assigned a staff to the Program accountant in order to maintain updated records.

Implementation Date: July 2005

Responsible Person: Mr. Ramón Figueroa Cortés
Federal Programs Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-04
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Allowable Costs/Cost Principles Reporting
Statement of Condition	The housing assistance payments expenditures reported in the HUD-52681, Vouchers for Payment of Annual Contributions and Operating Statement for the year ended June 30, 2004 included the housing assistance payments issued during the fiscal year 2003-2004 on behalf of portability participants administered by the Municipality. Also, the administrative fee income related to portability participants administered by the Municipality was not reported in the operating receipts section of the HUD-52681, Vouchers for Payment of Annual Contributions and Operating Statement for the year ended June 30, 2004.
Criteria	OMB Circular A-87, Attachment C, states that to be allowable under Federal awards, costs must be net of all applicable credits, such as receipt or reduction of expenditure-type transactions that offset or reduce expense items allocable to Federal awards as direct or indirect costs. Code of Federal Regulation 24, Subpart C, Section 85.20 (b) (1), require that accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or sub-grant. Also, Code of Federal Regulation 24, Subpart C, Section 85.20 (b) (2) states that the grantee must maintain records, which adequately identify the source and application of funds, provided for financially assisted activities.
Cause of Condition	The housing assistance payments issued during the fiscal year 2003-2004 on behalf of portability participants administered by the Municipality was recorded in the Housing Assistance Payment General Ledger expenditures account (4715). Also, the administrative fee income related to portability participants was not properly recorded in the General Ledger.
Effect of Condition	The Municipality submitted a Year-End Settlement Statement report with overstated expenditures and understated cash receipts, affecting the year end settlement results and the operating reserve balance.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **04-04 (continued)**

Recommendation We recommended to the Municipality Management to instruct the program accountant to follow financial management procedures established in the Voucher Program Guidebook-Housing Choice (7420.10G), Chapter 20, Financial Management.

Questioned Cost Approximately \$15,000

Management Response and Corrective Action The Municipality management gave instructions to program accountant to modify the general ledger accounts and to modify the accounting procedures in order to properly record the portability transactions (as illustrated in the Voucher Program Guidebook-Housing Choice (7420.10G), Chapter 20, Financial Management) to comply with the Program financial management and accounting requirements. Also, the accountant was instructed to revise past transactions and, to post in the books any accounting adjustment necessary to properly present the financial position and the results of operations of the Program.

Implementation Date: July 2005

Responsible Person: Mr. Ramón Figueroa Cortés
Federal Programs Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-05
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Cash Management
Statement of Condition	We realized the Cash Management Test and after our procedures, we found that the Municipality maintained during the current fiscal year an average cash balance in books of approximately \$376,146. At June 30, 2004, the cash balance in books was \$309,627; \$37,220 of these funds were from operating reserve at June 30, 2004, as determined in the preliminary year-end settlement; and the remaining \$272,407 was not identified by us with respects to its origin. Also, portability accounts receivable and payable of \$36,907 and \$6,341 respectively, and an underpayment of approximately \$40,411 were reported in the fiscal year 2003-04 preliminary year-end settlement. Also, during the twelve (12) month of the fiscal year 2003-2004, the PHA maintains a leasing ranging from 71% to 85%.
Criteria	OMB Common Rules, Subpart C, Section 85.20 (b) (7), which requires a cash management system, in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursement by the grantee.
Cause of Condition	The condition could be caused by cumulative effect of accounting errors in the past years and current years; errors such as reporting portability administered by the Municipality as HAP expenditures in the year-end settlements, non recognition of portability administrative fee earned in the year-end settlements, non recognition of recoveries from tenants and owners in the year-end settlements, non recognition of interest earned on operating reserve in the year-end settlement, etc.
Effect of Condition	The Municipality did not comply with the OMB Common Rules, Subpart C, Section 85.20, (b) (7).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 04-05 (continued)

Recommendation We recommend to the Municipality's Management to instruct the program accountant to review the accounting records and related transactions supporting documents for the current and past years in order to identify the cash balance respects to its origin, and later, to make any necessary adjusting journal entries to correct accounting records.

Questioned Costs None

Management Response and Corrective Action The Municipality's Management gave instructions to program accountant to revise past cash transactions and, to post in the books any accounting adjustment necessary to properly present the financial position and the results of operations of the Program.

Implementation Date: July 2005

Responsible Person: Mr. Ramón Figueroa Cortés
Federal Programs Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-06
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test - Selection from the Section 8 Waiting List
Statement of Condition	<p>During our Waiting List Test we noted the following conditions:</p> <ul style="list-style-type: none">a. The waiting list did not include the following information about each applicant: (a) qualifications for any local preferences; and (b) racial or ethnic designation of the head of household.b. In our examination of seven (7) files of families admitted to the program during the fiscal year 2003-2004, we observed that those participants completed an application form according to the method required by the Municipality and were entered into the waiting list from June 1999 to February 2003. Also, our examination of such participant's files revealed that it does contain documents and information showing that the Municipality gave local preference for selection of such families. But, due to the fact that the waiting list did not include the qualifications for any local preferences, we were unable to determine if applicants with the same local preferences were selected using the date and time of the application or use of a drawing or other random choice technique.
Criteria	Code of Federal Regulations 24, Sections 982.54 (d) and 982.201 through 982.207 states the waiting list procedures and that the selection from the waiting list generally occurs when the PHA notifies a family, whose names reaches the top of the waiting list, to come in to verify eligibility for admission.
Cause of Condition	The waiting list did not include all information required by Federal Regulation.
Effect of Condition	The Municipality may be in noncompliance with 24 CFR sections 982.54 (d) and 982.201 through 982.207.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **04-06 (continued)**

Questioned Costs **None**

Recommendation We recommend the Municipality's Management to instruct program staffs to include in the program waiting list the applicant qualification for any local preference (if applicable) and ethnic designation of the head of household.

**Management Response
and Corrective Action**

The Municipality will update the existing waiting list to include applicants qualification for any local preference (if applicable) and ethnic designation of the head of household.

Implementation Date: April 2005

Responsible Person: Mr. Ramón Figueroa Cortés
Federal Programs Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-07
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test - Reasonable Rent
Statement of Condition	In eight cases (8) cases the determination of reasonable rent (reasonable rent certification) was not duly documented.
Criteria	Code of Federal Regulations 24, Subpart K, Sections 982.507 and 982.158 (f) (7) states that the PHA may not approve a lease until the PHA determines that the initial rent to owner is a reasonable rent. The PHA must determine reasonable rent during the term of the contract: (a) before any increase in the rent to owner; and (b) at the HAP contract anniversary if there is a five percent decrease in the published Fair Market Rent in effect 60 days before the HAP contract anniversary. Also, the PHA must maintain records to document the basis for the determination that the rent paid to the owner is reasonable.
Cause of Condition	The PHA controls and procedures failed to assure that a reasonable rent determination was performed as required by the regulations.
Effect of Condition	The PHA is not in compliance with Code of Federal Regulations 24, Subpart K, Sections 982.507 and 982.158 (f) (7).
Recommendation	We recommend management to strengthen controls procedures to assure that the rent paid to the owners is reasonable and that appropriate documentation about the determination of reasonable rent has been maintained in the applicable participant's files.
Questioned Costs	None.
Management Response and Corrective Action	The Municipality Management gave instructions to the program Director in order to realize a reasonable rent study to be used in the reasonable rent determination, when applicable, as required by Program regulations.

Implementation Date: April 2005

Responsible Person: Mr. Ramón Figueroa Cortés
Federal Programs Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-08
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test - Housing Assistance Payment (HAP)
Statement of Condition	Our examination of fifteen (15) participant's files revealed that for ten (10) cases, the Housing Assistance Payment Register was not actualized at our audit procedures date.
Criteria	Code of Federal Regulations 24, section 982.158 states that the PHA's are required to maintain a HAP contract register or similar record in which to record the PHA's obligation for monthly HAP's. This record must provide information as to: the name and address of the family, the name and address of the owner, dwelling unit size, the beginning date of the lease term, the monthly rent payable to the owner, monthly rent payable by the family to the owner, and the monthly HAP. The record shall also provide data as to the date the family vacates and the number of days the unit is vacant, if any.
Cause of Condition	The PHA controls and procedures failed to assure that all HAP transactions will be recorded promptly in the HAP Register.
Effect of Condition	The PHA is not in compliance with Code of Federal Regulations 24, section 982.158.
Recommendation	We recommend to the Municipality management to strengthen controls procedures to assure that all HAP transactions will be recorded promptly in the HAP Register. Also, the Municipality could consider the use of computer software to maintain a HAP Register, instead of a manual basis Register.
Questioned Costs	None.
Management Response and Corrective Action	The Municipality management assigned a staff to the Program accountant in order to maintain updated records, including HAP Register. Implementation Date: March 2005 Responsible Person: Mr. Ramón Figueroa Cortés Federal Programs Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
03-05	14.218	<p><u>The Program maintained a monthly average cash balance of \$38,788 in books.</u></p> <p>The corrective action was taken.</p>
03-06	14.218	<p><u>There is no evidence that the Municipality's employee responsible of applying monitoring procedures review the weekly payrolls to assure that the contractor comply with prevailing wages rates; there is no evidence of submission for the weekly payrolls of January to April 2004; there is only one on site visit to one employee during the fiscal year 2002-03.</u></p> <p>The corrective action was taken.</p>
03-07	14.218	<p><u>The Program has not established adequate internal control procedures to assure that rehabilitations are duly completed as required by regulations and appropriate documentation is maintained.</u></p> <p>The corrective action was taken.</p>
03-08	14.218	<p><u>The cash on hand at the end of the reporting period (Federal Cash Transactions Report (SF-272)-line 11j) for the periods ended 9/30/02 and 3/31/03, isn't the beginning balance in the following quarter; In the period ended 3/31/03 the amount of credit withdrawals (line 11a) did not reconcile with the accounting records.</u></p> <p>The corrective action was taken.</p>
03-09	14.218	<p><u>There were no adequate and accurate records to account for additions or dispositions of property and equipment during the fiscal year 2003-2004. The Property Subsidiary Ledger maintained by the program wasn't updated since the year 2000.</u></p> <p>The corrective action was taken.</p>
03-10	14.871	<p><u>At June 30, 2003, the cash balance in book was \$347,028; \$105,340 of these funds was from HUD overpayment during the fiscal year 2002-03 as determined in the year-end settlement; \$65,632 was from operating reserve at June 30, 2004, as determined in the year-end</u></p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<u>settlement; and the remaining \$176,056 was not identified by us with respects to its origin.</u>
		<u>We noted that during the twelve (12) month of the fiscal year 2003-2004, the PHA maintains a leasing rate under 95%, and maintains an average leasing rate of 86% for the fiscal year. The PHA did not submit to HUD a revised requisition (Form 52663) to reduce the monthly advance.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-05.
03-11	14.218	<u>The Municipality did not maintain appropriate monitoring procedures to detect the exclusion of certain contract clauses.</u>
		The corrective action was taken.
03-12	14.871	<u>We were unable to determine if the report of Voucher for Payment of Annual Contributions and Operating Statement was made in accordance with the required accounting basis since the amounts in the report don't trace to the accounting records.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-03, 04-04 and 04-05.
03-13	14.871	<u>The Municipality did not have adequate internal control procedures to assure that the participant's files include all required documentation and releases required by federal agencies.</u>
		The corrective action was taken.
03-14	14.871	<u>The Federal Program Department did not maintain adequate controls to document the basis for the determination of the reasonable rent paid to the owner.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-07.
03-15	14.871	<u>The Management does not have adequate internal control procedures to assure that the leased units were subject to annual inspections.</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<u>supervisory quality control inspections and documented them in a unit inspection report.</u>
		The corrective action was taken.
03-16	14.871	<u>The Municipality did not maintain an up-to-date utility schedule for the audit period ending June 30, 2003. The last time the PHA reviewed its utility allowance schedule was in 1999.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-08.
03-17	14.871	<u>The PHA does not select the families from the top of the waiting list according with the PHA applicant selection policies. Also, we noted that six (6) participants admitted for first time during the fiscal year 2002-03, did not appear in the Waiting List.</u>
		Partial corrective action was taken. All of new admitted families have been selected from the waiting list. See corrective action planned on Finding 04-06.
03-18	14.871	<u>We noted that the PHA did not maintain supporting documentation to assure that the Form HUD 50058, Family Report was transmit electronically to HUD as required by Federal Regulation.</u>
		The corrective action was taken.
02-06	14.218	<u>The Municipality should strengthen it's procedures to minimize the time elapsed between the transfer of funds from the federal entity and the disbursements made by the Municipality.</u>
		The corrective action was taken.
02-07	14.218	<u>The Municipality should establish the following procedures: As certain that the housing unit deficiencies be corrected and incorporated into the rehabilitation contract; Realize pre-rehabilitation inspection describing the housing unit deficiencies to be corrected; Assign a staff to inspect the rehabilitation work upon completion to assure that is carried out in accordance with the time None established in the contract.</u>

COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		The corrective action was taken.
02-08	14.218	<u>The Municipality should implement procedures in order to assure that the report only present the total credit withdrawal during the covered period.</u>
		The corrective action was taken.
02-09	14.218	<u>The Municipality should perform a physical inventory in order to actualize the property subsidiary. In addition, we recommended strengthening it's internal control procedures in order to assure that the program maintains proper records and adequately safeguards for the equipment to comply with program requirements and regulations.</u>
		The corrective action was taken.
02-10	20.507	<u>The Municipality should strengthen it's procedures to minimize the time elapsed between the transfer of funds from the federal entity and the disbursements made by the Municipality.</u>
		The corrective action was taken.
02-11	20.507	<u>The Municipality should improve its record retention system in order to assure that the documents are available for audit procedures.</u>
		The corrective action was taken.
02-12	14.871	<u>The Municipality should strengthen it's procedures to minimize the time elapsed between the transfer of funds from the federal entity and the disbursements made by the Municipality. The management must submit a revised requisition (Form 52663) to HUD when the leasing rate does not exceeds the 95% in order to avoid an excessive adjusted cash balance in books.</u>
		No corrective action has been taken. See current year finding number 04-05.
02-13	14.871	<u>The Municipality should implement procedures in order to assure that all financial and programmatic reports are prepared in accordance</u>

COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<u>with the required accounting basis.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-03, 04-04 and 04-05.
02-14	14.871	<u>The Municipality should establish the following procedures: Implement internal control procedures to assure that the participant's files include complete and updated documentation as required by federal agencies.</u>
		The corrective action was taken.
02-15	14.871	<u>The Municipality should implement controls to assure appropriate documentation of the determination of reasonable rent is maintained in participants file.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-07.
02-16	14.871	<u>The Municipality should implement internal control procedures to assure that inspections are performed and properly documented in Form HUD 52580.</u>
		The corrective action was taken.
02-17	14.871	<u>The Municipality should implement internal control procedures to assure that in all cases they document their requirement of correction of any cited HQS deficiencies within 30 calendar days of the inspection and that they perform and document the re-inspections to assure that PHA-required repairs were completed.</u>
		The corrective action was taken.
02-18	14.871	<u>The Municipality should document properly the evidence of its utility allowance study to determine if there has been a change of 10% or more in the utility rate each year as established in the federal regulations.</u>
		No corrective action has been taken. See corrective action planned on Finding 04-08.

COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
02-19	14.871	<p><u>The Municipality should follow admission procedures established in the administrative plan. Also, we recommend the management to establish proper internal control so that the waiting list includes all information as required by Federal Regulations. This control must permit proper tracing of participants selected in the waiting list in order to assure the selection from the top of the waiting list.</u></p> <p>The corrective action was taken.</p>
01-04	14.218 14.855 14.857	<p><u>The Municipality did not maintain adequate cash management procedures.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
01-06	14.218	<p><u>No appropriate documentation on housing rehabilitation files</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
01-07	14.218	<p><u>Failure in the preparation of the Financial Report</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
01-08	14.855	<p><u>No appropriate documentation on tenant files</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
01-09	14.855 14.857	<p><u>The determination of reasonable rent was not documented in the participant file.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was</p>

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
01-10	14.855 14.857	submitted to the Federal clearinghouse. <u>The evidence of quality control inspections was not documented in the participant file.</u>
		The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
01-11	14.855 14.857	<u>Failure in document the PHA requires correction of any cited HQS deficiencies within 30 calendar days of the inspection.</u>
		The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.