

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

MUNICIPIO DE CAYEY
AUDITORIA 2006-2007
30 DE JUNIO DE 2007

OFFICE OF THE COMPTROLLER
GENERAL OF THE GOVERNMENT
SAN JUAN, PUERTO RICO
10000

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY
BASIC FINANCIAL STATEMENTS
WITH THE ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT
YEAR ENDED JUNE 30, 2007

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY
BASIC FINANCIAL STATEMENTS
WITH THE ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT
YEAR ENDED JUNE 30, 2007

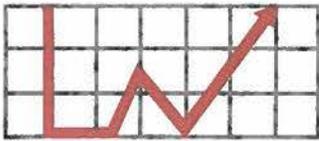
CONTENTS

	Page
<u>BASIC FINANCIAL STATEMENTS</u>	
Independent Auditors' Report	1-2
Required Supplementary Information (Part 1) Management's Discussion and Analysis	3-13
Government-Wide Financial Statements:	
Statement of Net Assets	14
Statement of Activities	15
Fund Financial Statements:	
Governmental Funds:	
Balance Sheet	16
Statement of Revenues, Expenditures and Changes in Fund Balances	17
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities	18
Notes to Basic Financial Statements	19-47
<u>SUPPLEMENTARY INFORMATION</u>	
Required Supplementary Information (Part II):	
Budgetary Comparison Schedule-General Fund	48
Notes to Budgetary Comparison Schedule-General Fund	49
Schedule of expenditures of federal awards	50-52
Notes to the schedule of expenditures of federal awards	53
<u>INTERNAL CONTROL AND COMPLIANCE WITH LAWS AND REGULATIONS</u>	
Report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with <i>Government Auditing Standards</i>	54-55

COMMONWEALTH OF PUERTO RICO
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BASIC FINANCIAL STATEMENTS
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YEAR ENDED JUNE 30, 2007

CONTENTS

	Page
<u>INTERNAL CONTROL AND COMPLIANCE WITH LAWS AND REGULATIONS (CONTINUED)</u>	
Report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with OMB Circular A-133	56-58
<u>FINDINGS AND QUESTIONED COSTS</u>	
Schedule of findings and questioned cost	59-72
Summary schedule of prior year audit findings	73-78



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 (Municipality)**, as of and for the year ended June 30, 2007, which collectively comprise the **Municipality's** basic financial statements as listed in the table of contents. These financial statements are the responsibility of the **Municipality's** management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements. An audit also includes assessing the accounting principles used and the 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 respective 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, 2007, 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.

INDEPENDENT AUDITORS' REPORT (CONTINUED)

In accordance with *Government Auditing Standards*, we have also issued our report dated October 3, 2007, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

The Management's Discussion and Analysis on pages 3 through 13 and the Budgetary Comparison Schedule-General Fund on page 48 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. 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.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
October 3, 2007

Stamp No. 2312111 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



Certified Public Accountants / Management Advisors

López-Vega, CPA, PSC

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2007

This discussion and analysis of the **Municipality of Cayey** (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2007. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2006. This MD & A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

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

FINANCIAL HIGHLIGHTS

The following comments about the financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2007 deserve special mention:

1. Total assets of the Municipality amounted to \$111,105,814 which represents an increase of 11% compared to prior fiscal year.
2. At the end of fiscal year 2007, total liabilities amounted to \$55,490,673. Out of said amount, \$44,773,493 corresponded to long-term liabilities of which \$33,409,000 represented the outstanding balance of bonds and notes issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.
3. Total net assets of the Municipality amounted to \$55,615,141 which represents an increase of 23% compared to prior fiscal year;

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

FINANCIAL HIGHLIGHTS (CONTINUED)

4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$43,053,474, derived from the following sources: \$3,337,783 charges for services; \$8,516,274 from operating grants and contributions; \$3,180,542 from capital grants and contributions obtained from other sources, and \$28,018,875 from general revenues available.
5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$32,741,005;
6. As reflected in the Statement of Activities, the current fiscal year operations contributed to an increase in the Net Assets figure by \$10,312,469;
7. As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$33,894,219;
8. As the end of the current fiscal year, the Municipality's general fund balance amounted to \$7,874,100, compared to a fund balance of \$2,972,935 in the prior fiscal year;
9. The actual General Fund budgetary activities resulted in a favorable balance of \$5,521,095.

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2007. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

Under the aforementioned approach, assets and liabilities are recognized using the accrual basis of accounting which is similar to the method used by most private enterprises. This means that current year's revenues and expenses are accounted for regardless of when cash is received or paid.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

FINANCIAL STATEMENTS COMPONENTS

The basic financial statements consist of the government wide financial statements, the major funds financial statements and the notes to the financial statements which provide details, disclosure and description of the most important items included in said statements.

The Statement of Net Assets reflects information of the Municipality as a whole of a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year. Such financial level is measured as the difference between total assets and liabilities, with the difference between both items reported as net assets. It is important to note that although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations. The higher the increments achieved in net revenues, the higher the capacity to increase the net assets figure either thru additional borrowings or thru internally generated funds. This in turn will benefit the welfare of Cayey constituents.

The Statement of Activities is focused on both gross and net cost of the various activities of the Municipality. It presents information which shows the changes in the Municipality's net assets at the most recent fiscal year. Based on the use of the accrual basis of accounting, changes are reported as soon as the underlying event occurs, regardless of the timing of the related cash flows. Under said approach, revenues and expenses are reported in the Statement of Activities based on the theory that it will result in cash flows to be realized in future periods.

A brief review of the Statements of Activities of the Municipality at June 30, 2007, shows total expenses incurred to afford the cost of all functions and programs amounted to \$32,741,005. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$15,034,599 was derived from the following sources: \$3,337,783 charges for services; \$8,516,274 from operating grants and contributions; and \$3,180,542 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$28,018,875. When such figure is added to the \$15,034,599 previously mentioned, total revenues available for the financing of activities amounted to \$43,053,474. There was an excess of revenues over expenses in the amount of \$10,312,469 which contributed with an increase to the figure of net assets attained at the end of the fiscal year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

The Fund Financial Statement is another important component of the Municipality's financial statements. A fund is a grouping of related accounts that are used to maintain accountability and controls over economic resources of the Municipality that have been segregated for specific activities. The Municipal fund type of accounting is used to demonstrate compliance with related legal requirements. Information offered thru this Statement is limited to the Municipality most significant funds and is particularly related to the local government only, instead of the government as a whole. Government funds are used to account for essentially the same functions as those reported as governmental activities. The funds are reported using an accounting method known as modified accrual accounting which measures cash and all other financial assets that can be readily converted into cash.

The fund statement approach gives the user a short term view of the Municipality's government operations and the basic services it provides. Since the focus of government funds is narrower than that of the financial statements as a whole, it also helps the user with comparable information presented in the governmental activities report. By doing so, readers of the basic financial statements may understand better the long-term effect of the Municipality's short-term financial decisions.

INFRASTRUCTURE ASSETS

Historically, a significant group of infrastructure assets such as roads, bridges, traffic signals, underground pipes not associated with utilities, have not been recognized nor depreciated in the accounting records of the Municipality. GASB 34 requires that such type of assets be inventoried, valued and reported under the governmental column of the Government-Wide Statement. The Municipality implemented the capitalization of infrastructure since July 1, 2002.

According to the requirements of GASB 34, the government must elect to either (a) depreciate the aforementioned assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery to near perpetuity. If the government develops the asset management system, (the modified approach) which periodically (at least every three years), by category, measures and demonstrate its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. In this particular respect, the Municipality has elected the use of recognizing depreciation under the useful life method and it contemplates to continue this treatment on said basis.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

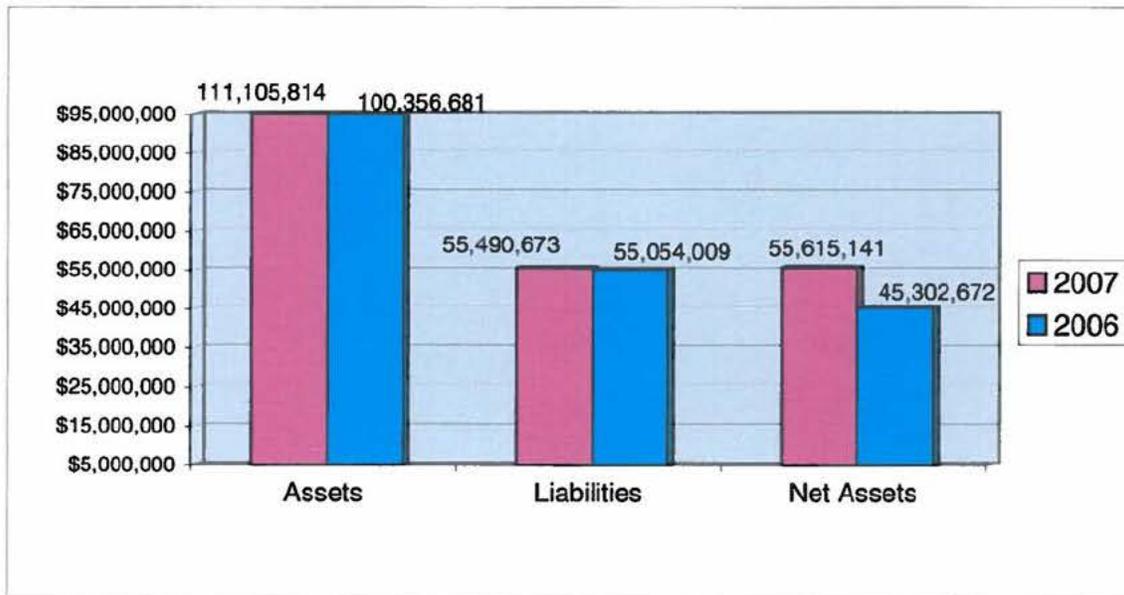
FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the **Municipality of Cayey**, primary government assets exceeded total liabilities by \$55,615,141 at the end of 2007, compared to \$45,302,672 at the end of the previous year, as showed in the following condensed Statement of Net Assets of the Primary Government.

Condensed Statement of Net

Assets	2007	2006	Change	%
Current assets	\$ 42,523,916	\$ 38,349,681	\$ 4,174,235	11%
Capital assets	68,581,898	62,007,000	6,574,898	11%
Total assets	111,105,814	100,356,681	10,749,133	11%
Current liabilities	10,717,180	9,088,424	1,628,756	18%
Noncurrent liabilities	44,773,493	45,965,585	(1,192,092)	(3%)
Total liabilities	55,490,673	55,054,009	436,664	1%
Invested in capital assets, net of related debt	35,172,898	27,012,000	8,160,898	30%
Restricted	26,286,340	26,913,363	(627,023)	(2%)
Unrestricted	(5,844,097)	(8,622,691)	2,778,594	(32%)
Total net assets	\$ 55,615,141	\$ 45,302,672	\$ 10,312,469	23%



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Approximately 53 percent of the Municipality's total revenue came from taxes, while 36 percent resulted from grants and contributions, including federal aid. Charges for Services provide 8 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for general government (39%), and health and welfare services (36%). 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.

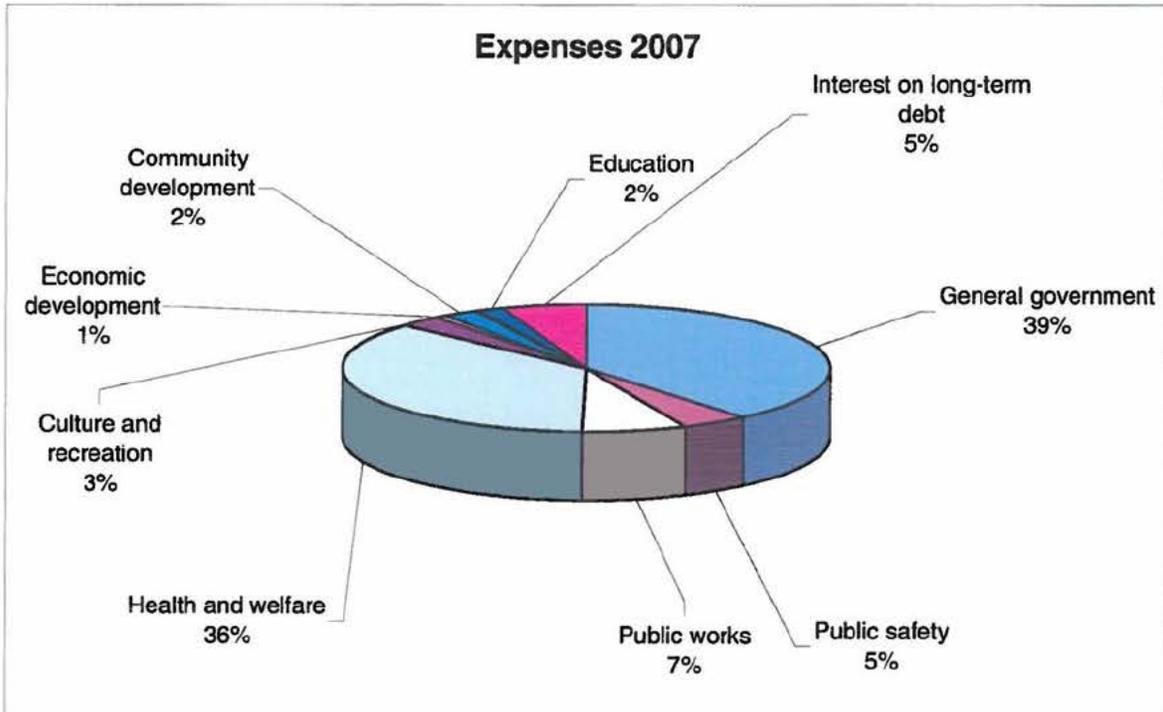
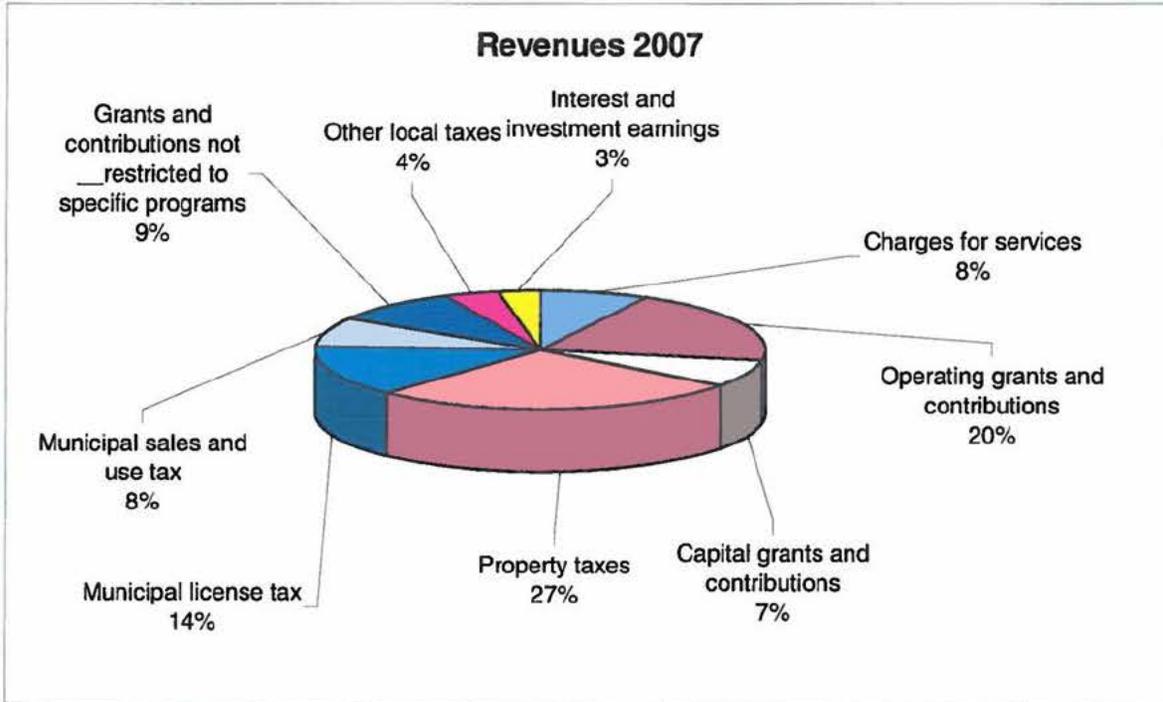
Condensed Statement of Activities	2007	2006	Change	%
Program revenues:				
Charges for services	\$ 3,337,783	\$ 3,118,976	\$ 218,807	7%
Operating grants and contributions	8,516,274	6,599,866	1,916,408	29%
Capital grants and contributions	3,180,542	3,988,787	(808,245)	(20%)
General revenues:				
Property taxes	11,402,122	10,820,175	581,947	5%
Municipal license tax	5,923,832	5,729,814	194,018	3%
Municipal sales and use tax	3,459,276	-	3,459,276	100%
Grants and contributions not restricted to specific programs	3,911,324	3,276,919	634,405	19%
Other local taxes	1,633,129	1,197,117	436,012	36%
Interest and investment earnings	1,328,612	1,040,025	288,587	28%
Miscellaneous	360,580	416,057	(55,477)	(13%)
Total revenues	43,053,474	36,187,736	6,865,738	19%
Expenses:				
General government	12,719,961	11,965,442	754,519	6%
Public safety	1,503,981	1,558,077	(54,096)	(3%)
Public works	2,260,345	5,346,607	(3,086,262)	(58%)
Health and welfare	11,911,542	10,898,569	1,012,973	9%
Culture and recreation	901,373	2,574,705	(1,673,332)	(65%)
Economic development	264,152	23,137	241,015	1042%
Community development	699,199	888,278	(189,079)	(21%)
Urban development	100,526	71,397	29,129	41%
Education	599,428	465,810	133,618	29%
Interest on long-term debt	1,780,498	1,551,398	229,100	15%
Total expenses	32,741,005	35,343,420	(2,602,415)	(7%)
Change in net assets	10,312,469	844,316	9,468,153	1121%
Net assets, beginning as restated	45,302,672	44,389,954	912,718	2%
Net assets, end of year	\$55,615,141	\$45,234,270	\$ 10,380,871	23%

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$33,894,219, an increase of \$3,939,519 in comparison with the prior year. There are reservations of fund balance amounting to \$28,162,089. This is the fund balance that it is not available for new spending because it has already been committed 1) \$1,875,749 to liquidate contracts and purchase orders of the prior fiscal year, 2) \$4,937,962 to pay debt service, 3) \$16,385,365 to pay for capital projects, and 4) \$4,963,013 for other purposes.

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2007, the general fund has an undesignated fund balance of \$5,732,130.

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.

The actual General Fund budgetary activities resulted in a favorable balance of \$5,521,095, caused mainly due to unexpected variances in revenue and expenditures.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2007, amounts to \$95,924,450, with an accumulated depreciation of \$27,342,552 (including depreciation charges for the year totaled \$2,193,908), leaving a net book value of \$68,581,898. This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure, furnishing, computers and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2007, the Municipality has \$6,195,206 of unexpended proceeds mainly from bonds and notes 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.

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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2007

CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State 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 fiscal year 2007-2008.

FINAL COMMENTS

The Municipality is an autonomous governmental entity whose powers and authority vested on its Executive and Legislative Branches are specifically established in the Municipal Autonomous Act approved in August 1991. By virtue of such powers, it provides a wide range of services to its constituents which includes, among others, public works, education, public safety, public housing, health, community development, recreation, waste disposal, welfare and others. The Municipality's principal sources of revenues are derived from property taxes, municipal license taxes, subsidies from the Commonwealth of Puerto Rico's General Fund and contributions from the Traditional and Electronic Lottery sponsored by said Government.

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. It further contemplates to maintain or improve its current levels of Net Assets as indicative of a strong financial position which has been identified as one of the main short and long-term objectives of the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2007

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, 2007

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 22,666,761
Cash with fiscal agent	13,289,245
Accounts receivable:	
Municipal license tax	23,142
Municipal sales and use tax	164,716
Intergovernmental	588,575
Interest	18,265
Federal grants	216,086
Others	87,517
Notes receivable	244,409
Other assets	5,225,200
Capital assets	
Land, improvements, and construction in progress	40,195,338
Other capital assets, net of depreciation	28,386,560
Total capital assets	<u>68,581,898</u>
Total assets	<u>111,105,814</u>
Liabilities	
Accounts payable and accrued liabilities	4,165,341
Due to other governmental entities	1,042,546
Deferred revenues:	
Municipal license tax	4,660,592
Federal grant revenues	848,701
Noncurrent liabilities:	
Due within one year	3,385,431
Due in more than one year	41,388,062
Total liabilities	<u>55,490,673</u>
Net Assets	
Invested in capital assets, net of related debt	35,172,898
Restricted for:	
Capital projects	16,385,365
Debt service	4,937,962
Other purposes	4,963,013
Unrestricted (deficit)	<u>(5,844,097)</u>
Total net assets	<u>\$ 55,615,141</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, 2007**

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	\$ 12,719,961	\$ 549	\$ -	\$ -	\$ (12,719,412)
Public safety	1,503,981	146,007	27,787		(1,330,187)
Public works	2,260,345	512,170	7,395	1,597,776	(143,004)
Health and welfare	11,911,542	2,673,211	7,239,413	37,911	(1,961,007)
Culture and recreation	901,373	5,846	52,290	149,694	(693,543)
Economic development	264,152		294,437	2,603	32,888
Community development	699,199			1,316,287	617,088
Urban development	100,526			76,271	(24,255)
Education	599,428		894,952		295,524
Interest on long-term debt	1,780,498				(1,780,498)
Total governmental activities	\$ 32,741,005	\$ 3,337,783	\$ 8,516,274	\$ 3,180,542	(17,706,406)
General revenues:					
Property taxes					11,402,122
Municipal license tax					5,923,832
Municipal sales and use tax					3,459,276
Other local taxes					1,633,129
Grants and contributions not restricted to specific programs					3,911,324
Interest and investment earnings					1,328,612
Miscellaneous					360,580
Total general revenues					28,018,875
Change in net assets					10,312,469
Net assets - beginning, as restated					45,302,672
Net assets - ending					\$ 55,615,141

Commonwealth of Puerto Rico
Municipality of Cayey
Balance Sheet
Governmental Funds
June 30, 2007

	General Fund	Special Revenue Fund - State & Local Grants	Special Revenue Fund Head Start	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Assets							
Cash and cash equivalents	\$ 13,874,444	\$ 3,883,623	\$ 160,074	\$ 4,254,740	\$ -	\$ 493,880	\$ 22,666,761
Cash with fiscal agent		1,122,173		6,516,865	4,904,554	745,653	13,289,245
Accounts receivable:							
Municipal license tax	23,142						23,142
Municipal sales and use tax	164,716						164,716
Intergovernmental	17,349	54,122		453,286	63,818		588,575
Interest					18,265		18,265
Federal grants			41,655			174,431	216,086
Others	87,517						87,517
Due from other funds	518,640					183,843	702,483
Notes receivable						244,409	244,409
Other assets	200			5,225,000			5,225,200
Total assets	\$ 14,686,008	\$ 5,059,918	\$ 201,729	\$ 16,449,891	\$ 4,986,637	\$ 1,842,216	\$ 43,226,399
Liabilities and Fund Balances							
Liabilities :							
Accounts payable and accrued liabilities	\$ 976,865	\$ 135,384	\$ 87,312	\$ 747,671	\$ -	\$ 130,626	\$ 2,077,858
Due to other governmental entities	1,042,546						1,042,546
Due to other funds	131,905	266,195	48,930		48,675	206,778	702,483
Deferred revenues:							
Municipal license tax	4,660,592						4,660,592
Federal grant revenues			65,487			783,214	848,701
Total liabilities	6,811,908	401,579	201,729	747,671	48,675	1,120,618	9,332,180
Fund balances:							
Reserved for:							
Encumbrances	1,875,749						1,875,749
Capital projects				15,702,220			15,702,220
Debt service fund					4,937,962		4,937,962
Other purposes	266,221	4,658,339					4,924,560
Reserved reported in nonmajor funds:							
Capital projects						683,145	683,145
Other purposes						38,453	38,453
Unreserved:							
Undesigned	5,732,130						5,732,130
Total fund balances	7,874,100	4,658,339	-	15,702,220	4,937,962	721,598	33,894,219
Total liabilities and fund balances	\$ 14,686,008	\$ 5,059,918	\$ 201,729	\$ 16,449,891	\$ 4,986,637	\$ 1,842,216	

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

Accrual basis of accounting accounts payable recognized in government-wide financial statements	(2,087,483)
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	68,581,898
Long-term liabilities are not due and payable in the current period, and therefore, are not reported in the funds	(44,773,493)

Net assets of governmental activities \$ 55,615,141

Commonwealth of Puerto Rico
Municipality of Cayey
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2007

	General Fund	Special Revenue Fund - State & Local Grants	Special Revenue Fund Head Start	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Revenues							
Property taxes	\$ 7,661,225	\$ -	\$ -	\$ -	\$ 4,007,824	\$ -	\$ 11,669,049
Municipal license taxes	5,923,832						5,923,832
Municipal sales and use tax	3,459,276						3,459,276
Licenses, permits and other local taxes	1,644,653						1,644,653
Charges for services	2,820,830						2,820,830
Intergovernmental	3,911,324	1,412,548		1,465,661		50,070	6,839,603
Fines and forfeitures	134,222						134,222
Rent of property	371,207						371,207
Interest	1,328,612						1,328,612
Federal grants			5,800,319			2,920,982	8,721,301
Miscellaneous	227,236					47,236	274,472
Total revenues	27,482,417	1,412,548	5,800,319	1,465,661	4,007,824	3,018,288	43,187,057
Expenditures							
Current:							
General government	11,914,043	106,721					12,020,764
Public safety	1,321,710					265	1,321,975
Public works	3,024,943	209,236		2,568,946		281,862	6,084,987
Health and welfare	4,289,392	9,364	5,800,319	2,328		1,589,652	11,691,055
Culture and recreation	758,736	26,525		2,038,221			2,823,482
Economic development		280,364		85,663			366,027
Community development	397,073	170,879				333,876	901,828
Urban development						76,271	76,271
Education	395,417	151,821		47,413			594,651
Debt service:							
Principal					3,091,000		3,091,000
Interest					1,780,498		1,780,498
Total expenditures	22,101,314	954,910	5,800,319	4,742,571	4,871,498	2,281,926	40,752,538
Excess (deficiency) of revenues over (under) expenditures	5,381,103	457,638		(3,276,910)	(863,674)	736,362	2,434,519
Other financing sources (uses)							
Transfers in		79,658		215,550	1,109,093	37	1,404,338
Transfers out	(479,938)					(924,400)	(1,404,338)
Long-term debt issued				1,505,000			1,505,000
Total other financing sources (uses)	(479,938)	79,658		1,720,550	1,109,093	(924,363)	1,505,000
Net change in fund balances	4,901,165	537,296		(1,556,360)	245,419	(188,001)	3,939,519
Fund balance, beginning as restated	2,972,935	4,121,043		17,258,580	4,692,543	909,599	29,954,700
Fund balance, ending	\$ 7,874,100	\$ 4,658,339	\$ -	\$ 15,702,220	\$ 4,937,962	\$ 721,598	\$ 33,894,219

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, 2007

Net Change in Fund Balances - Total Governmental Funds **\$ 3,939,519**

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. 8,661,961

Capital assets received as a donation are not recorded in the Governmental Funds, because current financial resources are not involved; however, the transaction must be reflected in the Government-Wide Financial Statements based on the fair value of the donated property. This is the amount of donated capital assets recorded in the current period. 133,344

Disposal of capital assets require removal of cost of the capital assets from the capital asset account on the Government-Wide Statement of Net Assets, resulting in a loss on disposal of capital assets on the Government-Wide Statement of Activities and Changes in Net Assets. (26,499)

Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Change 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. (2,193,908)

Bonds and notes proceeds provide current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide statement of Net Assets. Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long-term liabilities in the Government-Wide Statement of Net Assets. This is the amount by which the debt service principal payments exceed debt proceeds. 1,586,000

Repayment of long term property tax advance debt is an expenditure in Governmental Funds, but the repayment reduces long-term property tax advance debt in the Government-Wide Statement of Net Assets. The following amount represent the change in long-term property tax advance debt from prior year. 129,470

Long-term compensated absences are 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, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represent the change in long-term compensated absences from prior year. 209,027

Long-term claims and judgements are reported in the Governmental-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, claims and judgments are not reported as expenditures in Governmental Funds. The following amount represent the change in long-term claims and judgments from prior year. (827,788)

Long-term landfill obligation is reported in the Governmental-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, landfill obligation is not reported as expenditures in Government Funds. The following amount represent the change in long-term landfill obligation from prior year. 12,449

Repayment of long term Puerto Rico Electric Power Authority (PREPA) is an expenditure in Governmental Funds, but the repayment reduces long term PREPA in the Government-Wide Statement of Net Assets. The following amount represent the change in long term PREPA debt from prior year. 6,296

Repayment of long term Land Information Management System (LIMS) is an expenditure in Governmental Funds, but the repayment reduces long term LIMS in the Government-Wide Statement of Net Assets. The following amount represent the change in long term LIMS debt from prior year. 76,638

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenue in the funds. The following amount represents the change in this revenues from prior year. (266,925)

Expenses reported in the Government-Wide Statement of Activities and Change in Net Assets, but not reported as in the Governmental Funds because they do not require the use of current financial resources. The following amount represents the change in this expenses from prior year. (1,127,115)

Change in Net Assets of Governmental Activities **\$ 10,312,469**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2007

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 ("USGAAP") 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.). This requirement permits an optional four-year delay for implementation to fiscal year ended on June 30, 2007. The Municipality implemented the capitalization of infrastructure since July 1, 2002.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

The Following is a summary of the significant accounting policies of the Municipality:

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, as amended by the GASB Statement No. 39, "Determining Whether Certain Organizations Are Component Units an amendment of GASB Statement 14". 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. Based on the above criteria, the Municipality does not have component units to include within its reporting entity.

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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

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 grants and contributions that are restricted to meeting the operational or capital requirements of 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 & Local Grants- is the accounting entity in which revenues derived from local funds and state grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or state statutes.

Special Revenue Fund - Head Start- is the accounting entity, in which revenues derived from head start and child and adult care food program 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 - State & Local Grants - is the accounting entity in which revenues derived from local funds, and state 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 state statutes.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

Debt Service Fund - is the accounting entity used to account for the resources accumulated and payments made for principal and interest on long-term general obligation bonds of governmental funds.

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.

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

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

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

Special Revenue Fund – Head Start - Special Revenue Funds are used to account for revenues derived from head start and child and adult care food program funds. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

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

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

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

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

D. 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 ("USGAAP") 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, 2007

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

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, other 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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

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.

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 service 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. Also, cash with fiscal agent consists of unused proceeds of bonds and notes issued for the acquisition of equipment and construction of major capital improvements.

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 and federal grant receivable in the special revenue or capital project funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded or state founded programs. Intergovernmental 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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

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.

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:

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Buildings and site improvements	40 years	\$1
Infrastructure	40 years	\$1
Works of art	10 years	\$1
Vehicles	5 years	\$1
Furniture and fixtures	5 years	\$25
Machinery and equipment	3 to 5 years	\$25

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

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. All sick leave pay and salary related benefits are accrued when incurred in the governmental-wide financial statements when the employee meets such criteria.

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 when the liability is incurred.

8. **Reservations 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. **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.

b. **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.

c. **Other Purposes-** Represents net assets available for specific use and/or legally segregated for other specific future use.

d. **Debt Service Fund-** Represents net assets available to finance future debt service payments.

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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

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 gross property tax collections by the CRIM for the year ended June 30, 2007 amounted to approximately \$ 583,153. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$ 521,331 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</u> <u>Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 68,581,898	
Deduct:		
Bonds Payable	(27,949,000)	
Notes Payable	<u>(5,460,000)</u>	
		\$ 35,172,898
<u>Net assets restricted for capital projects</u>		
Capital projects fund - state & local grants - fund balance restricted for capital projects	15,702,220	
Other governmental funds - fund balance restricted for capital projects	<u>683,145</u>	
		16,385,365
<u>Net assets restricted for debt service</u>		
Debt service fund - fund balance		4,937,962

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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

Net assets restricted for other purposes

General fund – fund balance restricted for other purposes	266,221	
Special revenue fund – state & local grants- fund balance restricted for other purpose	4,658,339	
Other governmental funds – fund balance restricted for other purpose	<u>38,453</u>	4,963,013

Net assets unrestricted (deficit)

General fund – total fund balance:	\$ 7,874,100	
Deduct:		
Accrual basis accounts payable	(2,087,484)	
Fund balance restricted for other purposes	(266,221)	
Advances from CRIM	(4,935,019)	
Compensated absences	(2,812,843)	
Due to other governmental entity	(1,306,490)	
Claims and judgments	(846,688)	
LIMS repayment plan	(406,327)	
Landfill obligation	<u>(1,057,125)</u>	<u>(5,844,097)</u>
Total net assets – governmental activities		<u>\$ 55,615,141</u>

2. DEPOSITS

Under Commonwealth of 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 \$ 13,874,444 in the general fund, \$ 3,883,623 in the special revenue fund – state & local grants, \$160,074 in the special revenue fund – Head Start and \$ 4,254,740 in the capital projects fund – state & local grants were fully collateralized at June 30, 2007. In the other governmental funds there were deposits with commercial banks of \$ 493,880 that were fully collateralized.

The deposits at GDB of \$ 1,122,173 in the special revenue fund – state & local grants, \$ 6,516,865 in the capital projects fund – state & local grants, \$4,904,554 in the debt service fund and the \$ 745,653 in the other governmental funds, are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

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, 2007, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues
2. 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 of \$23,142 represents filed municipal license tax returns that were uncollected as of June 30, 2007, net of allowance for uncollectible accounts.

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

b. **Municipal Sales and Use Tax-** On May 25, 2006, the Municipal Legislature approved the Ordinance Number 125-2005-2006, which authorized the Mayor to impose a sales tax of 1.5%. This Ordinance was effective beginning on July 1, 2006. Municipal sales and use tax receivable of \$ 164,716 represents filed municipal sales and use tax returns that were uncollected as of June 30, 2007, net of allowance for uncollectible accounts.

c. **Intergovernmental Receivables-**

Intergovernmental receivable in special revenue fund - state & local grants represent expenditures incurred not yet reimbursed by other governmental entities. Following is a detail of the intergovernmental receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Commonwealth of Puerto Rico-Department of Labor and Human Resources- Law 52 Grant	\$ 54,122
Total	\$ 54,122

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

3. RECEIVABLES (CONTINUED)

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

<u>Governmental Entity</u>	<u>Amount</u>
Commonwealth of Puerto Rico-Legislature	\$ <u>453,286</u>
Total	\$ <u>453,286</u>

Intergovernmental receivable in the debt service fund represents property tax receivable at June 20, 2007. Following is a detail of the intergovernmental receivables:

<u>Governmental Entity</u>	<u>Amount</u>
Municipal Revenue Collection Center (CRIM)	\$ <u>63,818</u>
Total	\$ <u>63,818</u>

d. Federal Grants Receivables-

Federal grants receivable in special revenue fund - Head Start represent expenditures incurred not yet reimbursed by the pass-through grantor. Following is a detail of the federal grants receivable:

<u>Program Description</u>	<u>Amount</u>
Child and Adult Care Food Program	\$ <u>41,655</u>
Total	\$ <u>41,655</u>

Federal grants receivable in other governmental funds represent expenditures incurred not yet reimbursed by the Federal government or the pass-through grantors. Following is a detail of the federal grants receivable:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grants - Entitlement Grants	\$ 59,741
Child Care and Development Block Grant	18,999
Rural Housing Preservation Grant	71,594
Other programs	<u>24,097</u>
Total	\$ <u>174,431</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2007, and interfund transfers during the fiscal year ended at June 30, 2007, are summarized as follows:

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund - State & Local Grants	Payrolls, accruals, and other expenditures not reimbursed	\$ 266,195
General Fund	Special Revenue Fund - Head Start	Payrolls, accruals, and other expenditures not reimbursed	48,930
General Fund	Debt Service Fund	Interest Revenue	48,675
General Fund	Other Governmental Funds	Payrolls, accruals, and other expenditures not reimbursed	154,840
Other Governmental Funds	Other Governmental Funds	Reimbursable Expenditures	51,938
Other Governmental Funds	General Fund	Reimbursable Expenditures	<u>131,905</u>
Total			<u>\$ 702,483</u>

b. Transfer in/out to other fund

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund - State & Local Grants	Transfer of funds for special purpose	\$ 79,658
General Fund	Capital Projects Fund - State & Local Grants	Transfer of funds for capital outlays	214,358
General Fund	Debt Service Fund	Debt Retirement	185,885
General Fund	Other Governmental Funds	Transfer of funds for special purpose	37
Other Governmental Funds	Capital Projects Fund - State & Local Grants	Transfer of funds for capital outlays	1,192
Other Governmental Funds	Debt Service Fund	Debt Retirement	<u>923,208</u>
Total			<u>\$ 1,404,338</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

5. NOTES RECEIVABLE

At June 30, 2007, the notes receivable are composed of the following:

<u>Description</u>	<u>Amount</u>
Note receivable from "Cooperativa Agro-Comercial de P.R., La Marquetin", in the original amount of \$ 740,000, to be collected as follows:	
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.	<u>\$ 244,409</u>
Total	<u>\$ 244,409</u>

6. OTHER ASSETS

Other assets amounting to \$5,225,000 in the capital projects fund – state & local grants represent amount consigned in the state court for the acquisition of real property by expropriation.

7. CAPITAL ASSETS

Capital assets; those with an estimated useful live of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2007, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

7. CAPITAL ASSETS (CONTINUED)

<u>Governmental Activities:</u>	<u>Balance July 1, 2006</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance June 30, 2007</u>
Capital asset, not being depreciated:				
Land	\$ 19,795,214	\$ 133,344	\$ -	\$ 19,928,558
Construction in progress	<u>14,405,628</u>	<u>6,955,286</u>	<u>(1,094,134)</u>	<u>20,266,780</u>
Total capital assets not being depreciated	<u>\$ 34,200,842</u>	<u>7,088,630</u>	<u>(1,094,134)</u>	<u>40,195,338</u>
Capital assets, being depreciated:				
Buildings and buildings improvements	\$ 29,696,321	\$ 861,534	\$ -	\$ 30,557,855
Equipment	3,386,865	626,875	(28,945)	3,984,795
Infrastructure and infrastructure improvements	11,711,435	1,104,499		12,815,934
Work of art	7,500	7,500		7,500
Vehicles	<u>8,162,627</u>	<u>200,401</u>	<u>-</u>	<u>8,363,028</u>
Total capital assets being depreciated	<u>\$ 52,957,248</u>	<u>\$ 2,800,809</u>	<u>\$ (28,945)</u>	<u>\$ 55,729,112</u>
Less accumulated depreciation for:				
Buildings and buildings improvements	(12,860,824)	(554,132)	-	(13,414,956)
Equipment	(1,282,604)	(437,766)	2,446	(1,717,924)
Infrastructure and infrastructure improvements	(5,557,696)	(358,164)	-	(5,915,860)
Work of art	(625)	(625)	-	(625)
Vehicles	<u>(5,449,966)</u>	<u>(843,221)</u>	<u>-</u>	<u>(6,293,187)</u>
Total accumulated depreciation	<u>\$ (25,151,090)</u>	<u>\$(2,193,908)</u>	<u>\$ 2,446</u>	<u>(27,342,552)</u>
Total capital assets being depreciated, net	<u>\$ 27,806,158</u>	<u>\$ 606,901</u>	<u>\$ (26,499)</u>	<u>\$ 28,386,560</u>
Governmental activities capital assets, net	<u>\$ 62,007,000</u>	<u>\$ 7,695,531</u>	<u>\$(1,120,633)</u>	<u>\$ 68,581,898</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

7. CAPITAL ASSETS (CONTINUED)

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

<u>Governmental activities:</u>	<u>Amount</u>
General government	\$ 434,194
Public safety	173,051
Public works	854,265
Community development	119,897
Culture and recreation	299,605
Health and welfare	283,753
Urban development	24,255
Economic development	111
Education	<u>4,777</u>
Total depreciation expense-governmental activities	<u>\$ 2,193,908</u>

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2007 are summarized as follows:

<u>Description</u>	<u>General Fund</u>	<u>Special Revenue Fund - State & Local Grants</u>	<u>Special Revenue Fund - Head Start</u>	<u>Capital Projects Fund - State & Local Grants</u>	<u>Debt Service Fund</u>	<u>Other Governmental Fund</u>	<u>Total</u>
Accounts payable	\$ 339,129	\$ 135,384	\$ 87,312	\$ 747,671	\$ -	\$ 130,626	\$ 1,440,122
Accrued liabilities	<u>637,736</u>	-	-	-	-	-	<u>637,736</u>
Total	<u>\$ 976,865</u>	<u>\$ 135,384</u>	<u>\$ 87,312</u>	<u>\$ 747,671</u>	<u>\$ -</u>	<u>\$ 130,626</u>	<u>\$ 2,077,858</u>

9. DUE TO OTHER GOVERNMENTAL ENTITIES

The amounts due to other governmental entities in the general fund include the following:

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Aqueduct and Sewer Authority	\$ 18,869
General Services Administration	300
Puerto Rico Telephone Company	58,393
Department of Treasury	532,042
Internal Revenue Service	82,369
Department of Labor and Human Resources	33,177
Puerto Rico Electric Power Authority	<u>317,396</u>
Total	<u>\$ 1,042,546</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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

9. DUE TO OTHER GOVERNMENTAL ENTITIES (CONTINUED)

During the fiscal year 2001-2002, the Municipality authorized the CRIM to retain the corresponding portion for the financing project of Land Information Management System - LIMS, contracted by the CRIM. A total of \$777,289 is to be retained in a ten years period at an interest rate of 5.95%, until November 28, 2011. At June 30, 2007, the outstanding debt balance was \$ 406,327. This amount will be presented in the government wide statement of net assets.

10. DEFERRED REVENUES

a. **Municipal License Tax-** The deferred revenues of approximately \$ 4,660,592 in the general fund relates to municipal license tax collected in fiscal year 2006-07 that will be earned in fiscal year 2007-08.

b. **Federal Grants-** The deferred revenues presented in special revenue fund - head start represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the pass-through grantors are as follows:

<u>Program Description</u>	<u>Amount</u>
Head Start Program	\$ 65,487
Total	<u>\$ 65,487</u>

The deferred revenues presented in other governmental funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government or the pass-through grantors are as follows:

<u>Program Description</u>	<u>Amount</u>
Special Program for the Aging-Title III, Part B-Grants for Supportive Services and Senior Centers	\$ 20,563
Disaster Grants-Public Assistance	726,936
Other Programs	<u>35,715</u>
Total	<u>\$ 783,214</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

11. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the Municipal Revenue Collection Center (CRIM), a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomous 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. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the preliminary liquidation noting that the advances exceeded collections by \$ 29,553. This excess will not be funded with available expendable financial resources at June 30, 2007. Based on this, such amount was presented in the government-wide financial statements.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

11. PROPERTY TAXES (CONTINUED)

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

On June 26, 1997, Public Law No. 21 was enacted authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable or equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law No. 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities thru a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law.

The Statement of Net Assets includes an outstanding debt balance of \$4,063,827 and \$841,639, respectively, related to Law No. 42 and Law No. 146.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

11. PROPERTY TAXES (CONTINUED)

The annual tax rate is 9.33% for real property and 7.33% 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) 2.50% 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.

12. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2007, was as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds Payable	\$28,545,000	\$ 1,010,000	\$ (1,606,000)	\$27,949,000	\$1,808,000
Notes Payable	6,450,000	495,000	(1,485,000)	5,460,000	1,100,000
Advances from CRIM	5,064,490	29,553	(159,023)	4,935,020	71,166
Compensated Absences	3,021,870	133,902	(342,929)	2,812,843	325,000
Due to Other					
Governmental Entity	1,312,786		(6,296)	1,306,490	
Claims and Judgments	18,900	827,788		846,688	
LIMS Repayment Plan	482,965		(76,638)	406,327	81,265
Landfill Obligation	<u>1,069,574</u>	<u>-</u>	<u>(12,449)</u>	<u>1,057,125</u>	<u>-</u>
Total	<u>\$45,965,585</u>	<u>\$ 2,496,243</u>	<u>\$ (3,688,335)</u>	<u>\$44,773,493</u>	<u>\$3,385,431</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 \$1,010,000. Bonds payable outstanding at June 30, 2007 are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

12. LONG-TERM LIABILITIES (CONTINUED)

<u>Type of bonds</u>	<u>Maturity date</u>	<u>Original Amount</u>	<u>Range of Interest rates</u>	<u>Balance at June 30, 2007</u>
1993 Series	7-1-07	\$ 2,440,000	4.2% to 6.4%	\$ 285,000
1994 Series	1-1-18	663,000	5.0%	409,000
1994 Series	1-1-18	465,000	5.0%	281,000
1998 Series	7-1-07	280,000	6.0% to 7.5%	40,000
1998 Series	7-1-22	1,015,000	4.9% to 6.7%	840,000
1998 Series	7-1-13	1,990,000	4.9% to 6.7%	1,155,000
1999 Series	7-1-13	355,000	4.9% to 6.7%	210,000
1999 Series	7-1-13	3,705,000	4.9% to 6.7%	2,225,000
1999 Series	7-1-12	725,000	2.7% to 7.3%	400,000
1999 Series	7-1-23	685,000	2.7% to 7.3%	580,000
2000 Series	7-1-19	355,000	2.7% to 7.8%	285,000
2000 Series	7-1-14	1,765,000	2.7% to 7.8%	1,170,000
2001 Series	7-1-25	270,000	2.7% to 6.1%	240,000
2001 Series	7-1-25	1,010,000	2.7% to 6.1%	910,000
2002 Series	7-1-16	255,000	2.7% to 5.0%	200,000
2002 Series	7-1-16	1,120,000	2.7% to 5.0%	870,000
2002 Series	7-1-18	835,000	2.7% to 5.1%	685,000
2002 Series	7-1-16	125,000	2.7% to 5.0%	100,000
2002 Series	7-1-26	255,000	2.7% to 5.6%	230,000
2003 Series	7-1-17	235,000	4.2% to 5.0%	195,000
2003 Series	7-1-17	325,000	4.2% to 5.0%	265,000
2003 Series	7-1-17	85,000	4.2% to 5.0%	65,000
2003 Series	7-1-27	1,110,000	4.2% to 5.3%	1,030,000
2003 Series	7-1-27	1,415,000	4.2% to 5.3%	1,310,000
2003 Series	7-1-18	205,000	4.2% to 5.3%	185,000
2004 Series	7-1-13	120,000	4.2% to 5.0%	90,000
2004 Series	7-1-18	205,000	2.4% to 4.8%	175,000
2004 Series	7-1-28	140,000	2.4% to 5.3%	120,000
2004 Series	7-1-14	140,000	3.3% to 4.7%	125,000
2005 Series	7-1-29	160,000	3.3% to 5.3%	150,000
2005 Series	7-1-24	330,000	4.2% to 5.3%	310,000
2005 Series	7-1-29	1,210,000	4.2% to 5.3%	1,160,000
2005 Series	7-1-14	1,230,000	3.3% to 4.7%	1,035,000
2005 Series	7-1-14	1,698,000	3.2% to 5.0%	1,414,000
2006 Series	7-1-20	125,000	6.3% to 7.3%	120,000
2006 Series	7-1-30	135,000	4.2% to 5.3%	130,000
2006 Series	7-1-30	145,000	4.2% to 5.3%	140,000
2006 Series	7-1-30	305,000	4.2% to 5.3%	300,000
2006 Series	7-1-25	905,000	4.2% to 5.3%	880,000
2006 Series	7-1-20	1,010,000	4.2% to 4.8%	965,000
2006 Series	7-1-30	5,755,000	6.3% to 7.2%	5,660,000
2007 Series	7-1-16	1,010,000	6.6% to 7.3%	<u>1,010,000</u>
Total general obligation bonds				<u>\$ 27,949,000</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

12. LONG-TERM LIABILITIES (CONTINUED)

These bonds, except the 2005 Series \$ 1,698,000 bond, are payable from the special ad valorem property tax of 2.50% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes. The 2005 Series \$ 1,698,000 bond is payable with General Fund resources.

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

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2008	\$ 1,808,000	\$ 1,472,340
2009	1,582,000	1,377,752
2010	1,689,000	1,295,857
2011	1,796,000	1,206,651
2012	1,919,000	1,109,902
2013-2017	8,311,000	4,081,618
2018-2022	4,624,000	2,427,778
2023-2027	3,950,000	1,243,980
2028-2032	<u>2,270,000</u>	<u>261,609</u>
Total	<u>\$ 27,949,000</u>	<u>\$ 14,477,487</u>

- c. **Notes Payable-** The proceeds of the issuance of notes payables were used principally to pay debt incurred in prior years and to cover the expenditures of a special event. During the current year, the Municipality issued notes for approximately \$495,000. The notes are payable as follows:

<u>Type of notes</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest rates</u>	<u>Balance at June 30, 2007</u>
2002 Series	7-1-08	325,000	2.7% to 5.0%	110,000
2002 Series	7-1-08	205,000	2.7% to 5.0%	70,000
2003 Series	7-1-07	55,000	4.2% to 5.0%	15,000
2003 Series	7-1-07	270,000	4.2% to 5.0%	65,000
2003 Series	7-1-09	1,030,000	4.2% to 5.0%	500,000
2003 Series	7-1-09	745,000	4.2% to 5.0%	360,000
2004 Series	7-1-10	180,000	4.2% to 5.0%	110,000
2004 Series	7-1-08	265,000	2.4% to 4.4%	115,000
2004 Series	7-1-08	605,000	4.2% to 5.0%	265,000
2005 Series	7-1-09	135,000	3.3% to 4.4%	85,000
2007 Series	7-1-13	495,000	6.6% to 7.3%	495,000
Section 108 - 2000 Series	8-1-14	1,670,000	6.2% to 6.5%	900,000
Section 108 - 2000 Series	8-1-15	4,225,000	6.2% to 6.5%	<u>2,370,000</u>
Total notes payable				<u>\$ 5,460,000</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

12. LONG-TERM LIABILITIES (CONTINUED)

Except for the Section 108 notes, which are payable with Community Development Block Grant – Entitlement Program and General Fund sources of revenues, these notes are payable from the special ad valorem property tax of 2.50% 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 notes payable are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2008	\$ 1,100,000	\$ 320,443
2009	1,060,000	263,704
2010	810,000	211,108
2011	475,000	170,144
2012	450,000	136,370
2013-2017	<u>1,565,000</u>	<u>214,934</u>
Total	<u>\$ 5,460,000</u>	<u>\$ 1,316,704</u>

- d. **Advances from CRIM-** This amount represents the balance owed to the CRIM at June 30, 2007 will be repaid through a financing obtained by the CRIM with GDB.
- e. **Compensated Absences-** The government-wide statement of net assets includes approximately \$1,194,970 of accrued sick leave benefits, and approximately \$1,617,873 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.
- f. **Due to Other Governmental Entity-** This amount represents the balance owed to the Puerto Rico Electric Power Authority (PREPA) at June 30, 2007, resulting from prior year's excess of electricity consumption over in lieu of payment of taxes.
- g. **LIMS Repayment Plan-** This amount represents the balance owed to the CRIM at June 30, 2007, as described in Note 9.
- h. **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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

12. LONG-TERM LIABILITIES (CONTINUED)

Based on this study, the Municipality has recognized \$ 1,057,125 as the Municipality's estimated current cost for landfill closure and post-closure costs as of June 30, 2007. The annual estimate of post closure costs has been assessed approximately to be \$15,500 for a period of approximately 30 years. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. The balance of closure and post-closure costs are reported in the government-wide statement of net assets.

13. 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 OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

13. PENSION PLAN (CONTINUED)

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, 2007 recorded as pension expenditures were approximately \$ 475,116. This amount represented 100% of the required contribution.

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

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

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2007, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

14. RISK MANAGEMENT

The Property Division of the Municipality is responsible of assuring that the Municipality's property is properly insured. Annually, the Property Division compiles the information of all property owned and its respective market value. After evaluating this information, the Property Division submits the data regarding the Municipality's properties to the Area of Public Insurance at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities. Settled claims have not exceeded commercial coverage in any of the past three fiscal years.

15. COMMITMENTS AND CONTINGENCIES

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

With respect to pending and threatened litigation, the Municipality has reported liabilities of approximately \$ 846,688 for awarded and anticipated unfavorable judgments. This amount was included in the financial statements and represents the amount estimated as probable liability or a liability with a fixed or expected due date, which will require future available financial resources for its payment.

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 resources for its payment.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

16. PRIOR PERIOD ADJUSTMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

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

<u>Description</u>	<u>General Fund</u>	<u>Special Revenue Fund - State & Local Grants</u>	<u>Special Revenue Fund - Head Start</u>	<u>Capital Projects Fund - State & Local Grants</u>	<u>Debt Service Fund</u>	<u>Other Governmental Fund</u>	<u>Total</u>
Fund balance, beginning	\$2,972,935	\$ 4,121,043	\$ -	\$17,258,580	\$ 4,692,543	\$ 841,197	\$29,886,298
To corrected prior year federal grants receivable						57,170	57,170
Others adjustments	-	-	-	-	-	11,232	11,232
Fund balance, beginning as restated	<u>\$2,972,935</u>	<u>\$ 4,121,043</u>	<u>\$ -</u>	<u>\$17,258,580</u>	<u>\$ 4,692,543</u>	<u>\$ 909,599</u>	<u>\$29,954,700</u>

B. GOVERNMENTAL WIDE FINANCIAL STATEMENTS

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

<u>Description</u>	<u>Total</u>
Net assets, beginning	\$ 45,234,270
To correct prior year federal grants receivable	57,170
Others adjustments	<u>11,232</u>
Net assets, beginning as restated	<u>\$ 45,302,672</u>

17. SUBSEQUENT EVENTS

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

17. SUBSEQUENT EVENTS (CONTINUED)

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2007

	<u>Budgeted Amounts</u>		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 7,661,225	\$ 7,661,225	\$ 7,661,225	\$ -
Municipal license tax	6,050,000	6,050,000	5,918,794	(131,206)
Municipal sales and use tax		3,189,687	3,826,602	636,915
Licenses, permits and other local taxes	1,572,350	1,572,350	1,651,253	78,903
Intergovernmental	3,084,337	3,205,684	3,911,324	705,640
Charges for services	3,318,772	3,318,772	4,079,221	760,449
Fines and forfeitures	30,000	30,000	86,474	56,474
Interest	701,000	701,000	1,320,332	619,332
Rent of property	136,000	136,000	371,207	235,207
Miscellaneous	<u>180,000</u>	<u>718,966</u>	<u>200,266</u>	<u>(518,700)</u>
Total revenues	<u>22,733,684</u>	<u>26,583,684</u>	<u>29,026,698</u>	<u>2,443,014</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES				
Current:				
General government	11,602,366	14,246,454	12,764,722	1,481,732
Public safety	1,419,663	1,419,663	1,320,040	99,623
Public works	2,954,645	3,726,985	3,184,296	542,689
Culture and recreation	709,884	780,896	759,016	21,880
Health and welfare	4,923,309	5,147,915	4,485,423	662,492
Community development	511,791	512,652	397,073	115,579
Education	457,326	563,234	409,148	154,086
Operating transfer to other funds	<u>154,700</u>	<u>185,885</u>	<u>185,885</u>	<u>-</u>
Total expenditures, encumbrances and other financing sources	<u>\$ 22,733,684</u>	<u>\$ 26,583,684</u>	<u>23,505,603</u>	<u>3,078,081</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)			<u>\$ 5,521,095</u>	<u>\$ 5,521,095</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis)"available for appropriation" from the budgetary comparison schedule				\$ 29,026,698
Differences-budget to GAAP:				
GAAP adjustments to revenues				<u>(1,544,281)</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 27,482,417</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$ 23,505,603
Differences-budget to GAAP:				
Prior year encumbrances recorded as current year expenditures for GAAP basis				266,239
Current year encumbrances recorded as expenditures for budgetary purposes				(1,484,643)
Non budgeted transfer out				<u>294,053</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 22,581,252</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

NOTES TO BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2007

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 USGAAP, 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 USGAAP 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, 2007 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2007.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2007

<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		\$ 75,216
Pass-through the Commonwealth of Puerto Rico - Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	<u>547,268</u>
Total U.S. Department of Agriculture			<u>622,484</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Programs:			
Community Development Block Grants - Entitlement Grants	14.218		1,192,502
Urban Development Action Grants	14.221		96,056
Emergency Shelter Grants Program	14.231		36,368
Supportive Housing Program	14.235		20,288
Community Development Block Grants - Section 108 Loan Guarantee	14.248		64,582
Section 8 Housing Choice Voucher	14.871		978,259
Pass-through the Commonwealth of Puerto Rico - Municipality of San Juan:			
Housing Opportunities for Persons with AIDS	14.241	Not Available	<u>22,159</u>
Total U.S. Department of Housing and Urban Development			<u>2,410,214</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF TRANSPORTATION:			
Direct Programs:			
Federal Transit – Formula Grants	20.507		76,271
Total U.S. Department of Transportation			76,271
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	107,938
Pass-through the Commonwealth of Puerto Rico – Family Department:			
Community Service Block Grant	93.569	Not Available	12,797
Child Care and Development Block Grant	93.575	Not Available	106,755
Head Start Program	93.600	Not Available	5,275,514
Total U.S. Department of Health and Human Services			5,503,004
U.S DEPARTMENT OF HOMELAND SECURITY:			
Pass-through the Commonwealth of Puerto Rico – Governor Authorized Representative (GAR):			
Disaster Grants – Public Assistance	97.036	1247-DRPR 1501-DRPR 1552-DRPR	264,702

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
Hazard Mitigation Grant	97.039	Not Available	5,000
Pass-through the Commonwealth of Puerto Rico Governor Office - Public Security Affair Office: Homeland Security Grant Program	96.067	Not Available	<u>265</u>
Total U.S. Department of Homeland Security			<u>269,967</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 8,881,940</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, 2007

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 – Head Start, Debt Service Fund and in the Other Governmental 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:

Description	Special Revenue Fund Head Start	Debt Service Fund	Other Governmental Funds	Total
Per Schedule of Expenditures of Federal Awards	\$ 5,800,319	\$ 923,208	\$ 2,158,413	\$ 8,881,940
Non federal programs expenditures	-	<u>3,948,290</u>	<u>123,513</u>	<u>4,071,803</u>
Total expenditures in the fund financial statements	<u>\$ 5,800,319</u>	<u>\$ 4,871,498</u>	<u>\$ 2,281,926</u>	<u>\$ 12,953,743</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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

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

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Cayey, Puerto Rico**, as of and for the year ended June 30, 2007, which collectively comprise the **Municipality's** basic financial statements and have issued our report thereon dated October 3, 2007, 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.

Internal Control Over Financial Reporting

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

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the **Municipality of Cayey's** ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of **Municipality of Cayey's** financial statements that is more than inconsequential will not be prevented or detected by **Municipality of Cayey's** internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting, as item **07-01**.

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

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

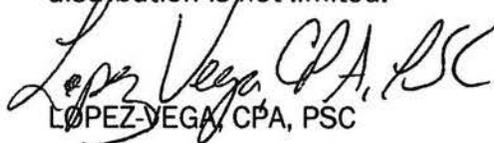
Compliance and Other Matters

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

We also noted certain other matters that we reported to management of the **Municipality of Cayey** in a separate letter dated October 3, 2007.

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

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
October 3, 2007

Stamp No. 2312112 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:

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- Puerto Rico Society of Certified Public Accountants

**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, 2007. The **Municipality of Cayey's** major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the **Municipality of 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 *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **Municipality of 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 of 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, 2007. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items **07-02** through **07-07**.

**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 the 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 the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of **Municipality of Cayey's** internal control over compliance.

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

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items **07-02** through **07-07** to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider items **07-03**, **07-04** and **07-06** to be material weaknesses.

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



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

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 8, 2008.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
March 8, 2008

Stamp No. 2312113 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, 2007

Section I – Summary of Auditor’s Results

Financial Statements

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

Federal awards

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

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
14.218	Community Development Block Grants - Entitlement Grants
14.871	Section 8 Housing Choice Voucher Program
93.600	Head Start Program

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section II – Financial Statements Findings

Finding Reference **07-01**

Requirement **Financial Reporting – Accounting Records**

Statement of Condition During our examination of the Municipality’s accounting system, we noted that it does not summarize the transactions in a formal General Ledger in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal funds). Also, the Municipality’s accounting system did not provide to produce its Governmental Wide Financial Statements.

Criteria Chapter VIII, Article 8.010 of 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’s 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’s 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 maintains two set of accounting records; a manual system and a computerized system provided in the past by the Office of the Commissioner of Municipal Affairs (OCAM). Actually, all of the transactions were recorded in both systems, but the manual system is the primary financial records for financial statements preparation purposes at the end of each fiscal year due to the fact that the computerized system real accounts balances carried forward from prior years were affected by accounting errors in the first years of the system operation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section II - Financial Statements Findings

Finding Reference **07-01 (Continued)**

Nevertheless, as part of the corrective action plan, the Commissioner of Municipal Affairs ("OCAM") consider alternatives to improve the accounting system, including the acquisition of new accounting software, and therefore, we will hope to solve our accounting system condition in a near future.

Implementation Date: January, 2009

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, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	07-02
Program	Community Development Block Grant-Entitlement Program (CFDA 14.218); U.S. Department of Housing and Urban Development
Requirement	Cash Management
Statement of Condition	During our cash management test, we noted that the Municipality requested funds that were not disbursed on a reasonable lapse of time. We selected a sample of eight (8) fund requisitions and found the following exception: a. In four (4) fund requisitions, we observed that the Municipality made the disbursements between six (6) and forty two (42) days after the deposits;
Criteria	OMB Common Rules, Subpart C, Section .20 (b) (7), 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 Municipality's disbursements procedures failed to assure that funds requested and received from the Federal agency be disbursed in compliance with the Code of Federal Regulations Requirements.
Effect of Condition	The Municipality is not in compliance with the OMB Common Rules, Subpart C, Section .20 (b) (7).
Recommendation	We recommend Management to strengthen its disbursement procedures to minimize the time elapsed between the transfer of funds from the Federal agency and the disbursements made by the Municipality.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **07-02 (Continued)**

**Management Response
and Corrective Action**

As part of our corrective action plan, we will instruct Program accounting staff, in order to strength control and procedures to assure that the conditions observed by the auditors does not occur again. We are going to start the disbursement process when the requisitions of funds are submitted to the U.S. Department of Housing and Urban Development (HUD), in order to assure that when the funds are transferred by the agency, the program will disburse them immediately.

Implementation Date: April, 2008

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	07-03
Program	Community Development Block Grant-Entitlement Program (CFDA 14.218); U.S. Department of Housing and Urban Development
Requirement	Davis-Bacon Act
Statement of Condition	During our Davis-Bacon Act test, we found the following exceptions: a) In four (4) construction projects, the contractor did not submit, on a timely basis, the required weekly payrolls. Therefore, monitoring procedures over those payrolls were not done promptly to verify its compliance with prevailing wage rates; b) In two (2) cases, there is no evidence that the contractor was informed in the procurement process of the requirements for Davis-Bacon Act. Also, in one (1) case, a contract includes a series of attachments relating to the Davis Bacon Act, nevertheless, no reference to them were included in the contract clauses; c) In one (1) case, there is no evidence of on-site visits performed to monitor classifications of workers and wage rates paid to them. In addition, in a monitoring visit performed by program staff, we identified three (3) employees interviewed that were not included in the project weekly payroll.
Criteria	Davis-Bacon Act, as amended DOL (40 USC 276a to 276a-7)
Cause of Condition	The Municipality's controls and procedures failed to apply all monitoring system procedures developed to test applicable contractors with respect to payment of prevailing wages.
Effect of Condition	The Municipality is not in compliance with Davis-Bacon Act, as amended DOL (40 USC 276a to 276a-7).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 07-03 (Continued)

Recommendation We recommend Management to follow monitoring system procedures developed, including the following:

- a) Informing contractors in the procurement process and prior to contractual agreement signature about the applicability of Davis Bacon Act;
- b) Through field on site visits;
- c) Realize contractors and subcontractors interviews, and;
- d) Obtaining contractor's and subcontractor's weekly payrolls to be reviewed on a weekly basis to establish the degree of compliance and the nature and extend of violations, if any, and then, communicate contractors promptly about any failure in the payroll process.

Questioned Costs None

**Management Response
and Corrective Action**

As part of our corrective action plan, we will establish a communication with the program staff in order to strengthen its monitoring system procedures related to compliance with Davis Bacon Act. Also, we will establish a communication with the Municipality's Engineering Office and with all contractors, in order to require the submittal of weekly payrolls on time.

Implementation Date: April, 2008

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	07-04
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 ended on June 30, 2007 did not present properly the financial position and the results of Program's operations.
Criteria	<p>OMB Common Rules, Subpart C, Part .20 (b) (2), Accounting records, 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 the necessary accounts to properly post cash and modified accrual basis transactions.
Effect of Condition	The Municipality is not in compliance with the OMB Common Rules, Subpart C, Part .20 (b) (2) and with the Voucher Program Guidebook-Housing Choice (7420.10G), Chapter 20.
Recommendation	<p>We recommended 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.</p> <p>Also, we recommended Management to follow the requirements included in the HUD PHA GAAP Conversion Guide, prepared by the U.S. Department of Housing and Urban Development's Real Estate Assessment Center (REAC).</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 07-04 (Continued)

Questioned Cost None

**Management Response
and Corrective Action**

As part of our corrective action plan, we contracted the service of accounting consultants, in order to acquire and implement a new accounting software (Peachtree Accounting Software). We hope that with the assistance of the external accounting consultants and following the HUD PHA GAAP Conversion Guide, prepared by the U.S. Department of Housing and Urban Development's REAC, we will convert our accounting records from HUD's basis of accounting to General Accepted Accounting Principles (GAAP).

Implementation Date: July, 2008

Responsible Person: Mr. Edwin Quiles
Finance Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	07-05
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Cash management
Statement of Condition	<p>We realized Cash Management Test and after our procedures, we found that during the current fiscal year, the Program maintained a monthly average cash balance in books of approximately \$116,031. Also, at June 30, 2007, the cash balance in book was \$140,517. We did not identify the origin of those funds.</p> <p>Also, the PHA maintained an average leasing rate of 89% instead a 95%, as required. This means that the Program did not use all vouchers approved to the Municipality.</p>
Criteria	<p>OMB Common Rules, Subpart C, Section .20 (b) (7), 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.</p> <p>Housing Choice Voucher Program Guidebook, Chapter 24, Section, 24.6 stated that a PHA must lease 95 percent of its units. A PHA with a utilization rate below 95 percent will not be identified as a high performer regardless of its overall score and will not be eligible to receive new unit's allocations.</p>
Cause of Condition	<p>The Municipality did not maintain appropriate cash management procedures in order to request funds to Federal agencies only for immediate needs. Also, the condition may be cause by cumulative effect of accounting errors in the past years.</p> <p>In addition, the Municipality did not maintain an occupancy rate of 95% during the fiscal year; however, it continued to receive funds consistent with a higher lease up.</p>
Effect of Condition	<p>The Municipality is not in compliance with the OMB Common Rules, Subpart C, Section .20 (b) (7) and with the Housing Choice Voucher Program Guidebook, Chapter 24, Section, 24.6.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	07-06
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Eligibility of Individuals
Statement of Condition	<p>We performed an eligibility test of fifteen (15) participant's files and found the following exceptions:</p> <ul style="list-style-type: none">a) In four (4) cases, the PHA did not use an updated Fair Market Rent Schedule for the HAP calculation;b) In two (2) cases, the PHA used an incorrect family income for the HAP calculation;c) In one (1) case, the PHA did not use the minimum rent for the HAP calculation;d) In one (1) case, the PHA used an incorrect utility allowance for the HAP calculation;e) In one (1) case, the PHA assigned an incorrect handicap deduction for the participant. As result, the Program paid an incorrect HAP to the owner and reimbursed an incorrect utility allowance to the participant.
Criteria	Code of Federal Regulations 24, Subpart K, and Section 982.505 establish the procedures to be followed to calculate the Housing Assistance Payment. The Housing Choice Voucher Guidebook, number 7420.10G, Chapter six (6) and the PHA Administrative Plan establish procedures to be used as part of the HAP calculation.
Cause of Condition	The PHA controls and procedures failed to assure that all HAP's payments are duly computed by the program staff.
Effect of Condition	The PHA is not in compliance with Code of Federal Regulations 24, Subpart K, Section 982.505 and with the Housing Choice Voucher Guidebook, number 7420.10G, Chapter six (6).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **07-06 (Continued)**

Recommendation We recommend the PHA to strengthen its monitoring procedures to assure the HAP's are duly computed as required by the Federal Regulations. Also, we recommend that the PHA must verify the tenant files to determine which families required adjustments in their rents or utility reimbursements, and adjust the same retroactively to the date of the last reexamination, if need.

Questioned Costs None

**Management Response
and Corrective Action** As part of our corrective action plan, we will strengthen our verification procedures in order to avoid in the future the situations mentioned by auditors in the statement of condition.

Implementation Date: April, 2008

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	07-07
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico – Family Department (ACUDEN)
Requirement	Cash Management
Statement of Condition	<p>We realized cash management test and examined five (5) cash advances received by the Municipality during the fiscal year 2006-2007. Also, we verified the bank statements and cash reconciliation for that period. The following summarizes the situations found:</p> <ul style="list-style-type: none">a. The Municipality requested funds that were not disbursed on a reasonable lapse of time;b. The Municipality maintains an average cash balance of \$115,229 during the fiscal year 2006-2007.
Criteria	<p>OMB Common Rules, Subpart C, Section .20 (b) (7), 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.</p>
Cause of Condition	<p>The procedures established by ACUDEN in the agreement of delegation of funds do not provide a clause to comply with this requirement.</p>
Effect of Condition	<p>The Municipality is not in compliance with OMB Common Rules, Subpart C, Section .20 (b) (7).</p>
Recommendation	<p>We recommend management to require ACUDEN alternate methods to request cash in order to comply with this requirement.</p>
Questioned Costs	<p>None</p>
Management Response And Corrective Action	<p>We will establish a communication with ACUDEN in order to strengthen cash management procedures to minimize the time elapsed between the transfer of funds from this Agency and the disbursements made by the Municipality.</p> <p>Implementation Date: April 1, 2008</p> <p>Responsible Person: Mrs. Idenisse Diaz Head Start Program Director</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2007

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
06-02	14.218	<p><u>During the Cash Management test, the auditors noted that the Municipality requested funds that were not disbursed on a reasonable lapse of time. In five (5) cases the disbursements were made from sixteen (16) to one hundred twenty three (123) days after receipt of funds.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 07-02.</p>
06-03	14.218	<p><u>During the Davis-Bacon Act test, the auditors found the following exceptions: (a) The Municipality did not monitor the classifications of the workers and wage rates paid in seven (7) of twenty two (22) weekly payrolls; (b) One (1) weekly payroll was not submitted by the contractor during the fiscal year 2005-2006; (c) The contract did not contain a provision for payment of prevailing wage rates as stated by the Davis Bacon Act.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 07-03.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
06-04	14.218	<p><u>During the contract provision test, the auditors examined one (1) construction contract, and one (1) professional service contract for the amounts of \$107,221 and \$7,000 respectively, and noted the following situations: (a) One (1) contract did not include a provision for compliance with Sections 103 and 107 of the Contract Work Hours & Safety Standards Act; (b) Two (2) contracts did not include a provision for granting access to GAO or other federal agency, to books and other documents; (c) One (1) contract did not include a provision for compliance with the Clean Air and Water Act; (d) One (1) contract did not include a provision for compliance with Energy Policy and Conservation Act; (d) One (1) contract did not include a provision for compliance with the Copeland "Anti-Kickback" Act; (e) Two (2) contracts did not include a provision for retention of all required records for three (3) years; (f) One (1) contract did not include a provision for compliance of Executive Order 11246 "Equal Employment Opportunity"; (f) One (1) contract did not include a provision for Davis Bacon Act.</u></p> <p>Corrective action was taken.</p>
06-05	14.871	<p><u>During the test, the auditors noted that the set of accounting records maintained for the fiscal year 2005-2006 did not present properly the financial position and the results of operations of the program.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 07-04.</p>
06-06	14.871	<p><u>During the test, the auditors noted that the PHA did not use an updated Fair Market Rent Schedule to calculate Housing Assistance Payment. As result, the Program paid an incorrect HAP to the owner and it caused differences in the amount of Tenants Rent to the owner.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 07-06.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
06-07	14.871	<p><u>In the Waiting List test, the auditors noted the following situation: (a) In fifteen (15) applicants included in the Waiting List, the auditors observed that the PHA did not maintain the required information to assure that the selection of new tenants admitted to the program were in accordance with the administrative plan; (b) The PHA did not have written policies in its administrative plan for selecting applicants from the waiting list; (c) Also, the "Waiting List" record book was damaged during the year and a new book was created. The auditors did not find evidence that demonstrated if the new book was created in the same order and with the same applicants included in the damaged book.</u></p> <p>Corrective action was taken.</p>
06-08	14.871	<p><u>The PHA did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2006. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten (10) percent or more in the utility rate.</u></p> <p>Corrective action was taken.</p>
06-09	14.871	<p><u>During the verification of nine (9) participant files, the auditors noted the following exceptions: (a) The Municipality did not perform the required Housing Quality Control re-inspections during the fiscal year 2005-2006.</u></p> <p>Corrective action was taken.</p>
06-10	93.600	<p>The auditors realized a Cash Management Test and found the following exceptions: (a) The program did not maintain the proper documentation (Audit Trail) necessary to reconcile the funds received from the pass-through grantor with the disbursement of checks.</p> <p>Corrective action was taken.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
05-02	14.218	<p><u>During the contract provision test, the auditors examined three (3) to construction contracts with a cost of \$181,472.15, \$170,629.65 and \$15,300 respectively, and noted the following situations: (a) Two (2) contracts did not include a provision for compliance with Sections 103 and 107 of the Contract Work Hours & Safety Standards Act; (b) Three (3) contracts did not include a provision for granting access to GAO or other federal agency, to books and other documents; (c) Two (2) contracts did not include a provision for compliance with the Clean Air and Water Act; (d) Three (3) contracts did not include a provision for compliance with Energy Policy and Conservation Act; (e) Two (2) contracts did not include a provision for compliance with the Copeland "Anti-Kickback" Act; (f) Three (3) contracts did not include a provision for retention of all required records for three (3) years; (g) Two (2) contracts did not include a provision for Executive Order 11246 "Equal Employment Opportunity"; (h) Two (2) contracts did not include a provision for Davis Bacon Act.</u></p> <p>Corrective action was taken.</p>
05-03	14.871	<p><u>During the examination, the auditors noted that the set of accounting records maintained for the fiscal year 2004-2005 did not present properly the financial position and the results of operations of the program.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 07-04.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
05-06	14.871	<p><u>During the Waiting List Test, the auditors noted the following conditions: (a) The waiting list did not include the following information about each applicant: (1) qualifications for any local preferences; and (2) racial or ethnic designation of the head of household; (b) In the examination of eight (8) files of participants admitted to the program during the fiscal year 2004-2005, the auditors 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 2004. Also, the 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, the auditors 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.</u></p> <p>Corrective action was taken.</p>
05-07	14.871	<p><u>During the Utility Allowance Schedule Test, the auditors noted the following: (a) The Municipality updated the Utility Allowance Schedule as of March 2005, but was not applied in the Housing Assistance Payment calculation during the following months of April through June 2005.</u></p> <p>Corrective action was taken.</p>
05-08	14.871	<p><u>During the verification of fifteen (15) participant files, the auditors noted that the Municipality did not perform the required Housing Quality Control re-inspections during the audit period.</u></p> <p>Corrective action was taken.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CAYEY**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2007

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
04-03	14.871	<p><u>The set of accounting records maintained by the Municipality for the fiscal year 2003-2004 did not present properly the financial position and the results of operations of the program</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>
04-06	14.871	<p><u>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. Also, in seven (7) files of families admitted to the program during the fiscal year 2003-2004, the 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, 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, the auditors 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.</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>