

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

MUNICIPIO DE CULEBRA
AUDITORIA 2011-2012
30 DE JUNIO DE 2012

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**



Oficina de Administración
de Asuntos Municipales
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**BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION**

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

**HON. WILLIAM I. SOLIS BERMUDEZ
MAYOR**

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION

FISCAL YEAR ENDED JUNE 30, 2012

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NIEVES VELAZQUEZ & CO., P.S.C.

Certified Public Accountants and Financial Consultants

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Municipality Legislative Body
Municipality of Culebra
Culebra, 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 Culebra as of and for the year ended June 30, 2012, 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 Governmental Audits 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Notes 1 and 4 to the financial statements, the Municipality does not record additions to capital assets nor has depreciation been recorded. Accounting principles generally accepted in the United States of America require that capital asset additions be capitalized and depreciated over their estimated useful lives, which would increase the assets, net assets and expenses of the governmental activities. The amount by which this departure would affect the assets, net assets and expenses of the governmental activities is not reasonably determinable.

As discussed in Note 8 to the financial statements, the Municipality did not comply with the requirement established by Statement No. 18, Accounting for Municipal Solid Waste Landfill Closure and Post-Closure Care Cost, issued by the Governmental Accounting Standards Boards and the regulation set forth by the U.S. Environment Protection Agency. At June 30, 2012, the accompanying statement of net assets does not include the required liability for closures and post-closure care costs of the Municipality's solid waste landfill. In addition, the expenses and result of operations reported in the statement of activities are understated and overstated, respectively, for amounts that could not be determined for the fiscal year ended June 30, 2012.

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INDEPENDENT AUDITOR'S REPORT
(Continued)

In our opinion, because of the effects of not capitalizing capital asset additions, not recording depreciation, and not recording and disclose landfill cost, as discussed in the third and fourth paragraphs, the financial statements referred to in the first paragraph do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the governmental activities of the Municipality of Culebra, and the changes in financial position thereof for the year then ended.

In addition, in our opinion, the financial statements referred to previously present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality of Culebra, as of June 30, 2012, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Governmental Auditing Standards, we have also issued our report dated April 30, 2013 on our consideration of the Municipality of Culebra' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements. 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Governmental Auditing Standards and important for assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information of the general fund on pages 3 through 9 and 47 through 48, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers them to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquires of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's financial statements as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the financial statements. The Schedule of Expenditures of Federal Awards is the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

April 30, 2013
San Juan, Puerto Rico

Stamp No. 2672777 of the Puerto Rico Society
of Certified Public Accountants
was affixed to the record copy of this report.



Nieves Velazquez & Co., P.S.C.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

The management of Municipality of **Culebra**, Puerto Rico (Municipality) offers this narrative overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2012. The Management's Discussion and Analysis (MD&A) is designed to focus on the current year activities, resulting changes and currently known facts, and much of the information is comparable to prior year. This MD&A should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements.

This MD&A is prepared in order to comply with the dispositions established in the Governmental Accounting Standards Board Statement No. 34 and, among other purposes, to provide the financial statements users with the following major information:

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

FINANCIAL HIGHLIGHTS

The following are key financial highlights for the fiscal year:

- ❖ The assets of the Municipality exceeded its liabilities at June 30, 2012 by \$8,287,502, and at June 30, 2011 by \$7,586,758, as restated;
- ❖ The Municipality's total net assets increased by \$700,744 during fiscal year 2011-2012;
- ❖ As of June 30, 2012, the Municipality's governmental funds reported combined ending fund balances of \$5,044,336, an increase of \$547,927 from the prior year;
- ❖ At June 30, 2012, the unrestricted deficit was \$2,001,993.
- ❖ The Municipality's capital assets inventory has no movement during fiscal year;
- ❖ The investment in capital assets for this year was not determinable;
- ❖ Loans principal payments were \$85,000 and \$115,000 in 2012 and 2011, respectively.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

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

GOVERNMENT-WIDE FINANCIAL STATEMENTS

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENT-WIDE FINANCIAL STATEMENTS (CONTINUED)

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

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

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

FUND FINANCIAL STATEMENTS

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Municipality, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

GOVERNMENTAL FUNDS

The Municipality's basic services are reported in the government fund financial statements. The government funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted into cash. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions.

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

NOTES TO THE BASIC FINANCIAL STATEMENTS

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

OTHER INFORMATION

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

GOVERNMENT-WIDE FINANCIAL ANALYSIS

GOVERNMENTAL NET ASSETS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Municipality, assets exceeded liabilities by \$8,287,502 as of June 30, 2012 versus \$7,586,758, as restated, as of June 30, 2011. Our analysis below focuses on the net assets (**Table 1**) and changes in net assets of the Municipality's governmental activities.

<u>Table 1</u> <u>Statement of Net Assets</u>	<u>2012</u>	<u>2011</u>
Current and non-current assets	\$ 5,664,513	\$ 5,186,178
Capital assets	<u>8,412,866</u>	<u>8,412,866</u>
Total Assets	<u>14,077,379</u>	<u>13,599,044</u>
Current liabilities	606,196	654,032
Long-term liabilities	<u>5,183,681</u>	<u>5,358,254</u>
Total Liabilities	<u>5,789,877</u>	<u>6,012,286</u>
Net assets:		
Investment in capital assets, net of related debt	6,047,866	6,352,866
Restricted	4,241,629	5,338,351
Deficit	<u>(2,001,993)</u>	<u>(4,104,459)</u>
Total Net Assets	<u>\$ 8,287,502</u>	<u>\$ 7,586,758</u>

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

GOVERNMENTAL ACTIVITIES

Governmental activities increased the Municipality's net assets. Key elements of this increase are as follows: the Municipality's governmental activities had net expenses of \$4,569,914. However, these services are intended to be primarily funded by taxes, as opposed to charges for services and grants, and those taxes and other general revenues exceed net expenses by \$700,744.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

GOVERNMENT-WIDE FINANCIAL ANALYSIS (CONTINUED)

GOVERNMENTAL ACTIVITIES (CONTINUED)

The Municipality experienced an increase in sales taxes and licenses and permits revenues. Also, a decreased in expenses of \$1,975,387 was reflected during fiscal year 2011-2012. The cost of all governmental activities this year was \$5,460,861. **Table 2** presents the cost of each of the Municipality's largest programs.

<u>Table 2</u> <u>Statement of Activities</u>	<u>2012</u>	<u>2011</u>
Revenues		
Grants and contributions	\$ 890,947	\$2,508,233
General revenues:		
Property taxes	616,359	697,733
Volume of business taxes	150,008	178,566
Sales taxes	1,473,648	1,385,539
Intergovernmental	2,666,208	2,696,155
Rent	18,762	19,788
Licenses and permits	239,322	225,337
Miscellaneous	<u>106,351</u>	<u>410,320</u>
Total revenues	<u>6,161,605</u>	<u>8,121,671</u>
Expenses		
General Government	2,470,743	2,637,108
Public Safety	138,422	200,649
Public Works	850,752	853,900
Culture and Recreation	180,564	153,875
Human Services and Welfare	403,844	660,250
Urban Development	1,187,488	2,662,151
Education	171,277	219,337
Interest on long-term debts	<u>57,771</u>	<u>48,978</u>
Total expenses	<u>5,460,861</u>	<u>7,436,248</u>
Changes in net assets	700,744	685,423
Net assets – beginning, as restated	<u>7,586,758</u>	<u>6,901,335</u>
Net assets – ending, as restated	<u>\$8,287,502</u>	<u>\$7,586,758</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENT FUND FINANCIAL ANALYSIS

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

Table 3			
Balance Sheet	2012	2011	
Assets:			
Total assets – Major Funds	\$7,488,353	\$7,570,803	
Total assets – Other Funds	<u>1,025,542</u>	<u>576,143</u>	
Combined total assets	<u>8,513,895</u>	<u>8,146,946</u>	
Liabilities:			
Total liabilities – Major Funds	2,529,270	3,159,182	
Total liabilities – Other Funds	<u>940,289</u>	<u>491,355</u>	
Combined total liabilities	<u>3,469,559</u>	<u>3,650,537</u>	
Fund Balances:			
Restricted – Major Funds	4,156,376	5,253,563	
Restricted – Other Funds	85,253	84,788	
Assigned – Major Funds	1,891,750	-	
Unrestricted – Major Funds	<u>(1,089,043)</u>	<u>(841,942)</u>	
Combined total fund balances	<u>5,044,336</u>	<u>4,496,409</u>	
Total liabilities and fund balances	<u>\$ 8,513,895</u>	<u>\$ 8,146,946</u>	

Table 4			
Changes in Fund Balances	2012	2011	
Revenues:			
Total revenues – Major Funds	\$5,337,566	\$7,564,480	
Total revenues – Other Funds	<u>845,795</u>	<u>521,454</u>	
Combined total revenues	<u>6,183,361</u>	<u>8,085,934</u>	
Expenditures:			
Total expenditures – Major Funds	4,792,279	7,987,690	
Total expenditures – Other Funds	<u>843,155</u>	<u>580,399</u>	
Combined total expenditures	<u>5,635,434</u>	<u>8,568,089</u>	
Other financing sources (uses):			
Proceed from issuance of bonds	-	400,000	
Transfer – In	2,175	15,927	
Transfer – Out	<u>(2,175)</u>	<u>(15,927)</u>	
Combined other financing sources (uses), net	<u>-</u>	<u>400,000</u>	
Net changes in fund balance	547,927	(82,155)	
Fund Balance – beginning, as restated	<u>4,496,409</u>	<u>4,578,564</u>	
Fund Balance – ending	<u>\$5,044,336</u>	<u>\$4,496,409</u>	

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

GOVERNMENTAL FUNDS

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of its fiscal year. At June 30, 2012, the Municipality's governmental funds reported combined ending fund balances of \$5,044,336, an increase of \$547,927 from the prior year.

The Municipality has an unrestricted fund deficit of \$1,089,043 in its General Fund. The remainder of the balance is reserved to indicate that it is not available for new spending because it has already been restricted; (a) to pay debt service \$1,503,756 and (b) for other restricted purposes \$4,629,623.

BUDGETARY HIGHLIGHTS

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

After the original budget is approved, it may be revised for a variety of reasons such as unforeseen circumstances and other unanticipated revenues. Differences between the original 2012 budget and the final amended budget for the General Fund were relatively minor and can be summarized as follows:

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

CAPITAL ASSETS AND DEBT ADMINISTRATION

The Municipality's investment in capital assets for its governmental type activities as of June 30, 2012 amounted to \$8,412,866 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, machinery and equipment, parks, roads and bridges. **Table 5** present the major classes of capital assets, which have not been updated since June 2010.

Capital Assets	Amount
Land	\$3,366,886
Buildings	4,846,452
Motor vehicles	197,793
Machinery and equipment	<u>1,735</u>
Total Assets	<u>\$8,412,866</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

LONG-TERM DEBT

At June 30, 2012 the Municipality had a total of \$5,183,681 in general obligations and other outstanding debts, as shown in **Table 6**. Of this amount, \$2,365,000 comprises debt backed by the full faith and credit of the government and \$2,818,681 is other obligations.

Table 6	
Long Term Debts	Amount
General obligations	\$ 2,365,000
Others	<u>2,818,681</u>
Total Long Term Debts	<u>\$ 5,183,681</u>

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

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

All of these factors were considered in preparing the Municipality's budget for the 2013 fiscal year. Some cost reductions helped fund improvements of existing facilities, public safety and works, economic development initiatives and human service improvements.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Municipality's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information contact the Municipality's Finance Department at (787) 742-3510.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**STATEMENT OF NET ASSETS
June 30, 2012**

	Governmental Activities
ASSETS:	
Cash	\$ 3,150,906
Cash with Fiscal Agent	1,916,562
Receivables (net):	
Property Tax	37,777
Sales Tax	7,371
Federal Grants	439,617
Intergovernmental	112,280
	5,664,513
Capital Assets:	
Property, Plant and Equipment	11,951,490
Accumulated Depreciation	(3,538,624)
Total Capital Assets	8,412,866
Total Assets	14,077,379
 LIABILITIES:	
Accounts Payable and Accrued Expense	216,395
Bonds Payable	85,000
Accrued Interest	29,986
Due to Governmental Units	5,137
Deferred Revenue	
Volume of Business Tax	106,568
Federal Grants	163,110
Long-Term Liabilities:	
Due within One Year	133,266
Due in More than One Year	5,050,415
Total Liabilities	5,789,877
 NET ASSETS	
Invested in Capital Assets, Net of Related Debt	6,047,866
Restricted for:	
Debt Service	1,503,756
Other Purposes	2,737,873
Unrestricted (Deficit)	(2,001,993)
Total Net Assets	\$ 8,287,502

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Mayor and Municipal Legislature	\$ (608,358)	-	-	-	(608,358)
General Government	(1,862,385)	-	-	-	(1,862,385)
Public Safety	(138,422)	-	-	-	(138,422)
Public Works	(514,695)	-	-	-	(514,695)
Culture and Recreation	(180,564)	-	-	-	(180,564)
Sanitation	(336,057)	-	-	-	(336,057)
Human Services and Welfare	(403,844)	-	161,939	-	(241,905)
Urban Development	(1,187,488)	-	-	555,021	(632,467)
Education	(171,277)	-	173,987	-	2,710
Interest on Long-Term Debt	(57,771)	-	-	-	(57,771)
Total Governmental Activities....	\$ (5,460,861)	-	335,926	555,021	(4,569,914)

General Revenues:

Taxes:

Property Taxes, levied for General Purposes	408,319
Property Taxes, levied for Debt Services	208,040
Volume of Business Taxes	150,008
Construction Taxes	239,322
Sales Taxes, levied for Other Purposes	1,198,930
Sales Taxes, levied for Debt Services	274,718
Intergovernmental	2,666,208
Rent	18,762
Miscellaneous	106,351
Total General Revenues	5,270,658

CHANGE IN NET ASSETS

Net Assets - Beginning of Year	7,586,758
NET ASSETS - END OF YEAR	\$ 8,287,502

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

BALANCE SHEET - GOVERNMENTAL FUNDS
June 30, 2012

	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Funds	Total Funds
ASSETS:					
Cash	\$ 2,521,074	486,238	-	143,594	3,150,906
Cash with Fiscal Agent	-	45,652	1,593,895	277,015	1,916,562
Receivables:					
Property Tax	13,981	-	23,796	-	37,777
Sales Tax	6,320	-	1,051	-	7,371
Federal Grants	-	-	-	439,617	439,617
Intergovernmental	-	4,618	-	107,662	112,280
Due from Other Funds	589,334	2,202,394	-	57,654	2,849,382
Total Assets	\$ 3,130,709	2,738,902	1,618,742	1,025,542	8,513,895
LIABILITIES AND FUND BALANCES:					
Liabilities:					
Accounts Payable and Accrued Liabilities	\$ 171,061	20,450	-	24,884	216,395
Bonds and Notes Payable	-	-	85,000	-	85,000
Accrued Interest	-	-	29,986	-	29,986
Due to Other Governmental Units	5,137	-	-	-	5,137
Due to Other Funds	2,031,255	65,832	-	752,295	2,849,382
Deferred Revenue:					
Volume of Business Tax	106,568	-	-	-	106,568
Property Tax	13,981	-	-	-	13,981
Federal Grants	-	-	-	163,110	163,110
Total Liabilities	2,328,002	86,282	114,986	940,289	3,469,559
Fund Balances:					
Restricted	-	2,652,620	1,503,756	85,253	4,241,629
Assigned	1,891,750	-	-	-	1,891,750
Unassigned	(1,089,043)	-	-	-	(1,089,043)
Total Fund Balances	802,707	2,652,620	1,503,756	85,253	5,044,336
TOTAL LIABILITIES AND FUND BALANCES	\$ 3,130,709	2,738,902	1,618,742	1,025,542	8,513,895

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Funds	Total Funds
REVENUES					
Property Taxes	\$ 408,319	-	208,040	-	616,359
Volume of Business Taxes	150,008	-	-	-	150,008
Sales Taxes	1,198,930	-	274,718	-	1,473,648
Federal Assistances	-	-	-	700,290	700,290
Intergovernmental	2,666,208	43,625	-	145,505	2,855,338
Licenses and Permits	239,322	-	-	-	239,322
Rent	18,762	-	-	-	18,762
Miscellaneous	128,107	1,527	-	-	129,634
Total Revenues	4,809,656	45,152	482,758	845,795	6,183,361
EXPENDITURES					
Current:					
Mayor and Municipal Legislature	608,358	-	-	-	608,358
General Government	1,951,958	-	-	-	1,951,958
Public Safety	138,422	-	-	-	138,422
Public Works	514,280	415	-	-	514,695
Culture and Recreation	180,564	-	-	-	180,564
Sanitation	336,057	-	-	-	336,057
Human Services and Welfare	241,905	-	-	161,939	403,844
Urban Development	328,188	349,361	-	509,939	1,187,488
Education	-	-	-	171,277	171,277
Debt Service:					
Principal	-	-	85,000	-	85,000
Interest and Other Charges	-	-	57,771	-	57,771
Total Expenditures	4,299,732	349,776	142,771	843,155	5,635,434
Excess (deficiency) of revenues over (under) expenditures	509,924	(304,624)	339,987	2,640	547,927
OTHER FINANCING SOURCES (USES)					
Proceed of Bond	-	-	-	-	-
Transfer- In	2,175	-	-	-	-
Transfer- Out	-	-	-	-	2,175
Total Other Financing Sources and Uses	2,175	-	-	(2,175)	(2,175)
Net Change in Fund Balances	512,099	(304,624)	339,987	465	547,927
Fund Balance - Beginning as Restated (Note 17)	290,608	2,957,244	1,163,769	84,788	4,496,409
Fund Balances - Ending	\$ 802,707	2,652,620	1,503,756	85,253	5,044,336

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Total Fund Balances – Governmental Funds **\$5,044,336**

Amounts reported for Governmental Activities in the Statement of Net Assets are different because:

Capital Assets used in governmental activities are not financial resources and therefore are not reported in the funds. In the current period, these amounts are:

Capital Assets	\$ 11,951,490	
Accumulated Depreciation	<u>(3,538,624)</u>	
Total Capital Assets		8,412,866

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

Municipal Revenue Collection Center	13,981
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Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:

General Bonds and Notes Payable	(2,365,000)	
Compensated Absences	(398,342)	
Law 42	(2,196,759)	
Law 146	(6,857)	
Health Insurance Administration	<u>(216,723)</u>	
Total Long-Term Liabilities		<u>(5,183,681)</u>

Total Net Assets of Governmental Activities **\$ 8,287,502**

See accompanying Notes to Basic Financial Statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Net Change in Fund Balances – Total Governmental Funds	\$547,927
Amounts reported for Governmental Activities in the Statement of Activities are different because:	
Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds	13,981
Revenues in the governmental funds that correspond to prior year resources are not recorded as revenue in the Statement of Activities	(35,737)
Repayment of debt proceeds principal is expenditure in the governmental funds, but the repayment reduces Long-Term Liabilities in the Statement of Net Assets. In the current year the repayments were.	85,000
Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These activities consist of:	
Decrease in Compensated Absences	32,751
Decrease in Law 42	54,499
Decrease in LIMS	1,980
Decrease in Law 146	<u>343</u>
Total Additional Expenditures	<u>89,573</u>
Change in Net Assets of Governmental Activities	<u>\$700,744</u>

See accompanying Notes to Basic Financial Statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of **Culebra**, Puerto Rico (Municipality) was founded in the year 1880, and operates as a governmental unit of the Commonwealth of Puerto Rico, under Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipality Act of the Commonwealth of Puerto Rico (Law No. 81)*.

The Municipality's governmental system consists of executive and legislative branches. The Constitution of the Commonwealth of Puerto Rico (the "Commonwealth") provides for the separation of powers of the executive, legislative and judicial branches. A Mayor, elected every four years by the citizens, exercises the executive power of the Municipality. The legislative power is exercised by the Municipal Legislature, which consists of 4 Legislators also elected every four years. The General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality, exercises the judiciary power.

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

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

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

In June 1999, GASB issued Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB No. 34). This statement established new financial reporting requirements for state and local governments. On July 1, 2002, the Municipality adopted the provisions of GASB No. 34 as well as other statements referred to below.

The accompanying basic financial statements present the financial position and the results of operations of the Municipality and its various funds and fund types. The basic financial statements are presented as of June 30, 2012, and for the fiscal year then ended. The more significant of these accounting policies are described below and, where appropriate, subsequent pronouncements will be referenced.

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

The required supplementary information, which consists of a management discussion and analysis (MD&A), is information presented along with, but separate from, the Municipality's basic financial statements. The MD&A is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the year ended June 30, 2012, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

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

The Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of the special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Definitions of other governmental fund types were also modified for clarity and consistency.

A. Financial Reporting Entity

The accompanying basic financial statements include all departments and organizations units whose funds are under the custody and control of the Municipality. In evaluating the Municipality as a reporting entity, management has addressed all the potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of GASBS No. 14.

The basic criteria for including a potential component unit within the reporting entity is if potential component units are financially accountable and other organizations for which the nature and significance of their relationship with the entity are such that exclusion would cause the Municipality's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) ability of the Municipality to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Municipality.

The relative importance of each criterion must be evaluated in light of specific circumstances in order to determine which components units are to be included as part of the reporting entity. Our specific evaluations of the criteria applicable to the Municipality indicate no organizations meet the criteria to be included as component units. Accordingly, these basic financial statements present only the Municipality as the reporting entity.

These financial statements present the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2012, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. Measurement Focus and Basis of Accounting

Government-Wide Financial Statements

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

Governmental Fund Financial Statements

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

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

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

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

Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- ❖ Employee's vested annual vacation and sick leave is recorded as expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2012, has been reported only in the government-wide financial statements.

C. Financial Statement Presentation

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

Government-Wide Financial Statements

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

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

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

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

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

The accompanying statement of activities presents the Municipality's results of operations by showing, how the Municipality's net assets or liabilities changed during the fiscal year ended June 30, 2012, using a net (expense) revenue format. This statement presents the cost of each function/program as well as the extent to which each of the Municipality's functions, programs or other services either contributes to or draws from the Municipality's general revenues (such as property taxes, volume of business taxes, sales taxes, construction excise taxes, etc.).

A function/program describes a group of activities that are aimed at accomplishing a major service or regulatory responsibility. The functions/programs reported in the accompanying basic financial statements are: (1) Mayor and Municipal Legislature, (2) General Government, (3) Public Safety, (4) Public Works, (5) Culture and Recreation, (6) Health and Sanitation, (7) Human Services and Welfare and, (8) Urban Development. The governmental operations of the Municipality's departments and operational units are classified within the following functions/programs in the accompanying basic financial statements:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

Mayor and Municipal Legislature:

Municipal Legislature
Mayor's Office

General Government:

Department of Finance
Department of Human Resources
Department of Municipal Secretary
Department of Internal Audit

Public Safety:

Department of Emergency Management – Civil Defense
Department of Municipal Police

Public Works:

Department of Public Works

Culture and Recreation:

Department of Sports and Recreation
Department of Art, Culture and Tourism

Sanitation:

Department of Recycling Services

Human Service and Welfare:

Department of Health
Department of Citizen Affairs

Urban Development:

Department of Planning and Development
Federal Programs Office

The statement of activities demonstrates the degree to which program revenues offset direct expenses of a given function/program or segments. Direct expenses are those that are clearly identifiable with a specific function, segment or operational unit. This statement reports revenues in three broad categories: (1) program revenues, (2) general revenues and, (3) special items.

Program revenues – These revenues are generated directly from a program itself or may come from parties outside the Municipality's taxpayers or citizens. In the statement of activities, program revenues reduce the costs (expenses) of the function/program to arrive at: (1) the net cost of the function/program that must be financed from the Municipality's general revenues or (2) the net program revenue that contributes to the Municipality's general revenues. The accompanying statement of activities separately reports the following categories of program revenues:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

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

Special items – These items consist of revenues arising from significant transactions or other events within the control of management that are either unusual in nature or infrequent in occurrence.

Extraordinary items consist of revenues arising from significant transactions or other events that are both unusual in nature and infrequent in occurrence.

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

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

The Municipality classifies the most significant portion of its activities as governmental activities in the accompanying GWFS. These are activities generally financed through taxes, intergovernmental revenues and other non-exchange revenues that can be used to support the Municipality's programs or services. These governmental activities are also generally reported in the FFS.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

The Municipality has no fiduciary activities, which are those in which the Municipality would be holding or managing net assets for specific individuals or other external parties in accordance with trust agreements or other custodial arrangements.

The Municipality has operations and activities that are financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public (expenses, including depreciation) is financed primarily through user charges; and where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Governmental Fund Financial Statements

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

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

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

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

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

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

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

State Assignment Fund – This is the fund used to account for all the transactions of the State Assignment by Legislature Resolutions. The primarily objectives of this assignments is the development of projects on communities, not-for-profit organizations and indirect assignment to persons of low and moderate income.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Financial Statement Presentation (Continued)

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

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

D. 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.

The Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of the special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Fund types are as follows:

General Fund – is the Municipality main operating fund used to account for and report all financial and reported resources and governmental activities, except for those required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) USGAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund. Its revenues consist mainly of taxes, licenses and permits, intergovernmental, charges for services and other.

Special Revenue Fund – is a governmental fund used to account for and report the proceeds of specific revenue sources that are legally restricted, committed or assigned to expenditure for specified purposes other than debt service or capital projects. Resources restricted or committed to expenditure for purposes normally financed from the general fund are generally accounted for in the general fund provided that all applicable legal requirements can be appropriately satisfied and the use of special revenue funds is not required unless they are legally mandated.

Debt Service Fund – is a governmental fund used to account for and report for the accumulation of financial resources that are restricted for, and the payment of, principal and interest for: (1) bonds payable for which debt service payments are legally mandated to be accounted for in a debt service fund and (2) certain special long-term obligations for which the Municipality is being accumulating financial resources in advance to pay principal and interest payments maturing in future years.

Capital Projects Fund – is a governmental fund used to account for and report financial resources that are restricted, committed or assigned to expenditure for capital outlays, including the acquisition or construction of major capital facilities, including those outlays financed by the general obligation bond proceeds (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments). The use of the capital projects funds has been limited to only for major capital acquisitions, construction or improvement activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as furniture, office equipment, vehicles and other minor capital assets or improvements) have been reported in the governmental fund from which financial resources were used for the payment.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

E. Fund Balances

According to the provisions of GASB Statement No. 54, the fund balances are reported in five categories:

- ❖ **Nonspendable** – Amounts that cannot be spent because they are: a) not in spendable form or b) legally or contractually required to be maintained intact. Due to the nature or form of the resources, they generally cannot be expected to be converted into cash or a spendable form.
- ❖ **Restricted** – Amounts are restricted by external parties (creditors, grantors, contributors or law/ regulations) of other governments or restricted by law through constitutional provisions or enabling legislation.
- ❖ **Committed** – Amounts that can only be used for a specific purpose pursuant to constraints imposed by formal action (ordinances or resolutions) of the Municipality's highest level of decision making authority (Municipal Legislature). The formal action must occur prior to the end of the reporting period, however, the amount may be determined in the subsequent period. These are self-imposed limitations on available resources. These committed amounts cannot be used for any other purpose unless the government removes or changes the specified use by taking the same level of action it employed to previously commit those amounts. These committed amounts would be approved and adopted by formal action of the Municipal Legislature.
- ❖ **Assigned** – Amounts that are constrained by the Municipality's intent to be used for specific purposes that are neither restricted nor committed. The intent will be expressed by the Municipal Legislature, the Mayor or by an official to which the Municipal Legislature delegates authority in conformity with the Autonomous Municipalities Law of Puerto Rico.
- ❖ **Unassigned** – Represent the residual classification for the Municipality's General Fund. Therefore, in order to calculate unassigned fund balance, total fund balance less nonspendable, restricted, committed and assigned equals unassigned fund balance. The resulting amount will be available for any purpose.

Negative fund balance amounts are assigned amounts reduced to the amount that will raise the fund balance to zero. Consequently, negative residual amounts is restricted, committed and assigned fund balance classifications have been reclassified to unassigned fund balances.

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely.

However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balance amounts as of and for the fiscal year ended June 30, 2012.

When an expenditure is incurred for purposes for which amounts are available in multiple fund balance classifications, the Municipality uses restricted resources first, and then unrestricted resources. Within unrestricted resources, the Municipality generally spends committed resources first, followed by assigned resources, and then unassigned resources.

At June 30, 2012, the accompanying fund financial statements reported fund balances as restricted, assigned and unassigned.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

F. Budgetary Data

The Municipality annually adopts the Budget Resolution for all operating funds of the Municipality except for certain restricted accounts of Proprietary Funds and Special Revenue Funds. Budgetary control is legally maintained at the fund level. The budget is prepared using the modified accrual basis of accounting with encumbrance included as budgetary basis expenditures. The Municipality's Budget Resolution provides transfer authority (1) to the Mayor and the Management and Budget Director, within and between departments and funds, as long as the total budget of the Municipality (net of interfund transfers) is not increased; (2) to the Management and Budget Director to implement grant budgets as the grant applications are accepted by the Municipality; and (3) to the Management and Budget Director to amend (re-appropriate) each new year's budget, to the extent of outstanding encumbrances, and/or unexpended project/grant appropriations at year end. Municipality's Legislature action is required for (1) use of the budgeted Legislature contingency, and (2) the approval of supplemental appropriations. During the year, several supplemental appropriations were necessary.

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

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

1. Prior of May 31 of each fiscal year, the Mayor submits to the Municipal Legislature a proposed budget for the fiscal year commencing the following July 1 in addition of a budget message;
2. The budget document is available for public inspection prior to its approval by the Municipal Legislature;
3. The Commissioner of Municipal Affairs examines the budget to verify if it complied with the law's standards and sends it to the Mayor for any comments or recommendation before the limited date establishes by the Law;
4. Prior to June 13, the annual budget is legally enacted through passage of the annual appropriation ordinance;
5. If a budget is not adopted prior to the end of the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Municipal Legislature and the Mayor, is automatically renewed for the ensuing fiscal year until a new budget is approved. This permits the Municipality to continue making payments for its operating and other expenses until the new budget is approved;
6. Subsequent to the enactment of the annual appropriation ordinance, the Municipal Legislature has the authority to make necessary amendments made during the fiscal year and are reflected in the budget information included in the Budgetary Comparison Schedule – General Fund;
7. Budgetary data for the Special Revenue Fund has not been presented in the accompanying basic financial statements as such funds are budgeted over the life of the respective grant or project and not on an annual basis.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

F. Budgetary Data (Continued)

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

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. Cash, Cash Equivalent and Investment

The Finance Director of the Municipality is responsible for investing the available resources in certificates of deposit and other short-term investments. Investments are made from the available combined funds of the Municipality and, accordingly, it is not practical to disclose certificates of deposit and other short-term investments individually by fund in the combined financial statements. Interest earned on certificates of deposit and other short-term investments are recognized as revenue in the General Fund. Cash in the Special Revenue, Debt Service and Capital Project Funds are restricted; accordingly, resources available were not used for pool investments. At June 30, 2012, the Municipality does not have any type of investment.

Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the federal depository insurance generally provided by the Federal Deposit Insurance Corporation (FDIC). All securities pledged as collateral are held by agents designated by the Commonwealth's Secretary of the Treasury, but not in the Municipality's name.

Cash with fiscal agent represents property tax collections retained by the Municipal Revenues Collection Center and undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico.

Cash balance recognized in the Debt Service Fund is restricted for the payment of the Municipality's obligations, and others are restricted for specific projects, such as the acquisition or construction of permanent improvements. The sinking fund is maintained by the Governmental Development Bank of Puerto Rico, agency which acts as the insurer and payer of the Municipality's bonds and notes issued in accordance with law.

H. Receivables

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

I. Inventories

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

J. Capital Assets

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

J. Capital Assets (Continued)

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

Capital Assets	Years
Buildings and site improvements	20-50
Infrastructure	20-50
Vehicles	5-10
Machinery and equipment	5-20

The Municipality has not updated the additions, retirements and depreciation capital assets and, therefore, is not complying with GASB 34.

K. Long-Term Obligations

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

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

L. Compensated Absences

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

M. Compensated Absences (Continued)

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

The following is a summary of changes in the balance of Compensated Absences for the fiscal year ended June 30, 2012.

<u>BALANCE JULY 1, 2011</u>	<u>NEW ISSUES</u>	<u>RETIREMENTS AND CURRENT MATURATES</u>	<u>BALANCE JUNE 30, 2012</u>	<u>CURRENT PORTION</u>	<u>LONG-TERM PORTION</u>
<u>\$431,093</u>	<u>-----</u>	<u>32,751</u>	<u>398,342</u>	<u>25,000</u>	<u>373,342</u>

N. Insurance

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

O. Interfund Transactions

Interfund transactions are reflected as loans, reimbursements or transfers. Loans are reported as receivables and payables as appropriate and are subject to elimination upon consolidation. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the government-wide columnar presentation. The Municipality has the following types of reciprocal and nonreciprocal interfund activities:

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. Claims and Judgments

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

Q. Use of Estimates

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

R. Accounting for Pension Costs

For the purpose of applying the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers* (GASB No. 27), the state government of the Commonwealth of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multi-employer cost-sharing defined benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Commonwealth of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Commonwealth of Puerto Rico. Accordingly, no portion of the net pension obligation (NPO) related to ERS has been allocated to the Municipality in the accompanying basic financial statements. The basic financial statements of the Commonwealth of Puerto Rico report the total amount of the net pension obligation of ERS, including any amount that may correspond to the Municipality.

The Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

S. Risk Financing

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

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2012 amounted to \$78,571. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$73,398 for workers compensation insurance covering all municipal employees.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

T. Future Adoption of Accounting Pronouncements

The GASB has issued the following accounting standards that have effective dates after June 30, 2012:

- ❖ GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*. This statement is effective for periods beginning after December 31, 2012;
- ❖ GASB Statement No. 61, *The Financial Reporting Entity: Omnibus- an amendment of GASB Statements No. 14 and No. 34*. This statement is effective for periods beginning after June 30, 2013;
- ❖ GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre- November 30, 1989 FASB and AICPA Pronouncements*. This statement is effective for periods beginning after December 31, 2012;
- ❖ GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. This statement is effective for periods beginning after December 31, 2011;
- ❖ GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions (an amendment of GASB Statement No. 53)*. This statement is effective for periods beginning after June 30, 2013;
- ❖ GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement is effective for periods beginning after December 15, 2012.
- ❖ GASB Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*. This statement is effective for periods beginning after December 15, 2012.
- ❖ GASB Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25*.
- ❖ GASB Statement No. 68 *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*. This statement is effective for periods beginning after June 15, 2014.
- ❖ GASB Statement No. 69 *Government Combinations and Disposals of Government Operations*. The requirements of this statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis.

Except for GASB Statement No. 63, the Municipality's management has concluded that the future adoption of these GASB Statements will not have a significant impact on the basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 2 – CASH AND CASH EQUIVALENTS

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

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

Credit risk – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2012.

Interest rate risk – This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2012, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. At June 30, 2012, the Municipality's investments in certificates of deposits are recorded at cost, which approximates their fair value. Therefore, the Municipality's management has concluded that at June 30, 2012, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

Custodial credit risk – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$250,000 per depositor. In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2012. Therefore, the Municipality's management has concluded that at June 30, 2012 the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

Foreign exchange risk – The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2012.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

The Municipality's bank balances in commercial banks of \$2,521,074 in the General Fund and \$486,238 in the State Assignment Fund were fully collateralized at June 30, 2012. In the Other Governmental Funds there were deposits with commercial banks of \$143,594 that were fully collateralized.

The deposits at GDB of \$45,652 in the State Assignment Fund, \$1,593,895 in the Debt Service Fund and \$277,015 in the Other Governmental Fund, are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

NOTE 3 – RECEIVABLES

A. Federal Grants Receivable

Federal grants receivable in Other Governmental Funds represent expenditures incurred not yet reimbursed by the federal agencies or the pass-through grantors. Following is a detail of the federal grants receivable:

<u>Description</u>	<u>Amount</u>
Community Development Block Grant – State Program	\$226,814
Child Care Development Block Grant	189,974
Special Programs for the Aging Title III-Part B	<u>22,829</u>
Total	<u>\$439,617</u>

B. State Government Receivables

State government receivables represent expenditures incurred not yet reimbursed by the state agencies. Following is a detail of the state government receivables:

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Port Authority	\$ 4,618
State Department of Labor and Human Resources – Law 52	<u>107,662</u>
Total	<u>\$112,280</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 3 – RECEIVABLES (CONTINUED)

C. Due From and Due To Other Funds

Interfund receivables and payables at June 30, 2012 are summarized as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed	\$ 523,502
General Fund	State Assignment Fund	Payroll and related accruals paid and not reimbursed	65,832
State Assignment Fund	General Fund	Loans between funds	1,973,601
State Assignment Fund	Other Governmental Funds	Loans between funds	228,793
Other Governmental Funds	General Fund	Cash pool in the same bank account	<u>57,654</u>
Total			<u>\$ 2,849,382</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 4 – 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 2012, including those changes pursuant to the implementation of GASB Statement No. 34, follows (Land and construction in progress are not subject to depreciation):

Governmental Activities	Balance June 30, 2011	Additions	Retirements / Reclassifications	Balance June 30, 2012
Capital asset, not being depreciated:				
Land	\$ 3,366,886	-	-	\$ 3,366,886
Construction in progress	-	-	-	-
Total capital assets not being depreciated	<u>3,366,886</u>	-	-	<u>3,366,886</u>
Capital assets, being depreciated:				
Buildings	6,285,605	-	-	6,285,605
Infrastructure	-	-	-	-
Machinery and equipment	672,604	-	-	672,604
Motor vehicles	<u>1,626,395</u>	-	-	<u>1,626,395</u>
Total capital assets being depreciated	<u>8,584,604</u>	-	-	<u>8,584,604</u>
Less accumulated depreciation for:				
Buildings	(1,439,153)	-	-	(1,439,153)
Infrastructure	-	-	-	-
Machinery and equipment	(670,869)	-	-	(670,869)
Motor vehicles	<u>(1,428,602)</u>	-	-	<u>(1,428,602)</u>
Total accumulated depreciation	<u>(3,538,624)</u>	-	-	<u>(3,538,624)</u>
Total capital assets being depreciated, net	<u>5,045,980</u>	-	-	<u>5,045,980</u>
Governmental activities capital assets, net	<u>\$ 8,412,866</u>	-	-	<u>\$ 8,412,866</u>

Depreciation expenses were not charged to the governmental functions/programs:

Governmental activities	Amount
General Government	\$ -
Urban Development	-
Education	-
Public Safety	-
Public Works	-
Culture and Recreation	-
Human Services and Welfare	-
Total depreciation expenses	<u>\$ -</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 4 – CAPITAL ASSETS (CONTINUED)

GASB Statement No. 34 requires to retroactively applying the requirements to major general infrastructure assets within at least four (4) years of the adoption of this pronouncement, which is not later than June 30, 2007. The Municipality has not updated the additions, retirements and depreciation capital assets and, therefore, is not complied with GASB Statement No. 34.

NOTE 5 – ACCOUNTS PAYABLE AND ACCRUED EXPENSES LIABILITIES

Accounts payable and accrued expenses liabilities in governmental fund financial statements represent expenditures incurred during fiscal year 2011-2012, and not paid by the Municipality at June 30, 2012. Following is a detail of these accounts payable and accrued liabilities:

Major Governmental Funds	Accounts Payable	Accrued Liabilities	Total
General Fund	\$100,193	70,868	171,061
State Assignment Fund	20,450	-	20,450
Other Governmental Fund	<u>24,884</u>	-	<u>24,884</u>
Total	<u>\$145,527</u>	<u>70,868</u>	<u>216,395</u>

NOTE 6 – DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2012, balance due to other governmental units consists of the following:

Governmental Agency	Amount
Aqueduct and Sewer Authority	\$1,250
General Service Administration	<u>3,887</u>
Total	<u>\$5,137</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 7 – DEFERRED REVENUES

- A. The deferred revenues of \$106,568 in the General Fund relates to the volume of business tax collected in fiscal year 2011-2012 that will be earned in fiscal year 2012-2013. In addition, the \$13,981 in the General Fund are the property taxes that represents advances from fiscal year 2011-2012, not collected by the Municipality at June 30, 2012.
- B. **Federal Grants** – The deferred revenues presented in Other Governmental Funds represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Child Care Food Program	\$ 39,285
Public Assistance Grants	118,277
Child Care Development Block Grant-ARRA	77
Homelessness Prevention and Rapid Re-housing Program- ARRA	553
Energy Efficiency and Conservation Block Grant- ARRA	1,540
Rural Development	<u>3,378</u>
Total	<u>\$163,110</u>

NOTE 8 – GENERAL LONG-TERM DEBTS

Long-term liability activity for the year ended June 30, 2012, was as follows:

<u>Description</u>	<u>Beginning Balance, as restated</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds and Notes Payable	\$2,450,000	-	85,000	2,365,000	50,000
Property Tax Debt – Law 42	2,251,258	-	54,499	2,196,759	57,923
Compensated absences	431,093	-	32,751	398,342	25,000
LIMS Repayment Plan	1,980	-	1,980	-	-
Property Tax Debt – Law 146	7,200	-	343	6,857	343
Health Insurance Administration	<u>216,723</u>	-	-	<u>216,723</u>	-
Total	<u>\$5,358,254</u>	<u>-</u>	<u>174,573</u>	<u>\$5,183,681</u>	<u>\$133,266</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 8 – GENERAL LONG-TERM DEBTS (CONTINUED)

A. GENERAL OBLIGATIONS BONDS AND NOTES

The Municipality issues general and special obligation bonds and notes, principally, to provide funds for the acquisition and construction of major capital facilities, to pay debt incurred in prior years, and to cover the expenditures of a special event. Bonds and notes payables as of June 30, 2012, are comprised of the following individual issues:

DESCRIPTION	AMOUNT
\$2,125,000, Series 2009, for construction purposes, payable in annual installments ranging from \$30,000 to \$175,000, excluding interests from 1.55% to 7.50%, through July 1, 2033	\$1,985,000
\$400,000, Series 2011, for operational purposes, payable in annual installments ranging from \$10,000 to \$35,000, excluding interests from 6.00% to 7.50%, through July 1, 2031	<u>380,000</u>
Total General Obligations – Bonds	<u>\$2,365,000</u>

These bonds and notes are payable with the following Municipality's resources:

- ❖ Special ad valorem property tax, which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes and;
- ❖ Municipal sales taxes resources restricted for debt service.

B. BONDS AND NOTES AMORTIZATION

The annual requirements to amortize the general obligations outstanding as of June 30, 2012 are as follows:

Year Ending June 30,	Principal payment	Interest payment	Total
2013	\$ 50,000	134,339	184,339
2014	55,000	173,626	228,626
2015	60,000	169,500	229,500
2016	60,000	165,000	225,000
2017	70,000	160,500	230,500
2018-2022	430,000	716,256	1,146,256
2023-2027	610,000	530,256	1,140,256
2028-2032	855,000	261,378	1,116,378
2033-2037	<u>175,000</u>	<u>13,126</u>	<u>188,126</u>
Total	<u>\$2,365,000</u>	<u>2,323,981</u>	<u>4,688,981</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 8 – GENERAL LONG-TERM DEBTS (CONTINUED)

C. PROPERTY TAX DEBT – LAW 42

The Municipality entered into a repayment agreement with the Government Development Bank for Puerto Rico (GDB) and the CRIM, to pay off the excess of property tax advances through fiscal year 2000 and 2001. The CRIM retains the payment from the property tax advances of the Municipality. The amounts retained by the CRIM are remitted to GDB on July 1 of each year through July 1, 2032. The outstanding balance of the note payable to the CRIM at June 30, 2012 amounted to \$2,138,836.

D. COMPENSATED ABSENCES

The government-wide statement of net assets includes \$398,342 of accrued sick leave benefits, and accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

E. PROPERTY TAX DEBT – LAW 146

On September 24, 2002, the CRIM, on behalf of the municipalities of Puerto Rico, entered into a financing agreement with GDB pursuant to the provisions of Law No. 146 of October 11, 2001. The purpose of this financing agreement was to extinguish in advance certain bonds payable issued by the Public Finance Corporation, a subsidiary of the GDB, which were originally issued to pay certain property tax receivables owned by the municipalities of Puerto Rico through 1996. The outstanding balance of the note payable to the CRIM at June 30, 2012 amounted to \$6,857.

F. HEALTH INSURANCE ADMINISTRATION

Liabilities of \$216,723 reported in the statement of net assets represent the balance owed for services provided by the State Insurance Health Administration to the Municipality and not paid at June 30, 2012.

G. LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS OBLIGATION

The Municipality owns a municipal solid waste landfill. However, the Municipality has not adopted the required provisions of Statement No. 18, *Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs*, issued by the Governmental Accounting Standards Board (GASB No. 18) and the regulations set forth by the U.S. Environmental Protection Agency (EPA) in its "Solid Waste Disposal Facility Criteria", issued on October 9, 1991. According to these standard and regulations, the Municipality is required to place a final cover on its landfill site when closed and perform certain maintenance and monitoring functions at the landfill site for 30 years after closure. Although closure and post-closure care costs will be paid only near or after the date that the landfill stops accepting waste, the Municipality is required to report a portion of these closure and post-closure care costs as an operating expense in each period based on landfill capacity used as of each statement of net assets date. The accompanying statement of net assets does not include the required liability for closure and post-closure care costs of the solid waste landfill using current cost allocated based on the actual landfill capacity used at June 30, 2012.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 9 – DEBT RETIREMENT

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

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

NOTE 10 – PROPERTY TAXES

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

Personal property taxes are self-assessed by taxpayers every year generally using the book value of personal property assets owned by the taxpayer at January 1 (assessment date) and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. The total personal property tax rate in force at June 30, 2012 was 6.83% (of which taxpayers pay 5.80% and 1.03% is reimbursed by the Department of Treasury).

Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property deflated to 1957 market prices. The total real property tax rate in force at June 30, 2012 was 8.83% (of which 7.80% is paid by taxpayers and 1.03% is also reimbursed by the Department of Treasury).

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

CRIM is responsible for the billing and collections of real and personal property taxes on behalf of the Municipality. Prior to the beginning of each fiscal year, CRIM informs the Municipality of the estimated amount of property tax expected to be collected for the ensuing fiscal year. Throughout the year, CRIM advances funds to the Municipality based on the initial estimated collections. CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers.

This settlement has to be completed on a preliminary basis not later than each December 31. If CRIM remits to the Municipality property tax advances, which are less than the property tax actually collected, an additional property tax receivable is recorded at June 30. However, if advances exceed the amount actually collected by CRIM, an intergovernmental payable is recorded at June 30.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 10 – PROPERTY TAXES (CONTINUED)

In addition, 1.50% of the total personal and real property taxes collected by CRIM is restricted for the Municipality's debt service requirements and is retained by GDB for such purposes.

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

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

NOTE 11 – VOLUME OF BUSINESS TAXES

The Municipality is authorized by Law No. 81 to impose and collect municipal license taxes on all trade or business activities operated by any natural or legal person within the territorial area of Culebra. This is a self-assessed tax generally based on the business volume measured by gross sales. The Municipality establishes the applicable tax rates. At June 30, 2012, the municipal tax rates imposed by the Municipality were 1.50% for financing institutions and 0.50% for other types of taxpayers. Any taxpayers that have been granted with partial tax exemptions under any of the incentive tax laws of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60% and 90% under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return to be filed every April 15 based on the actual volume of business generated in the preceding calendar year.

Taxpayers with a sales volume of \$3 million or more must include audited financial statements with their tax returns. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration.

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

Any municipal license taxes collected in advance (that is, pertaining to a future fiscal year) are recorded as deferred revenues in the GWFS and the GFFS (See Note 7).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 12 – SALES TAXES

On July 4, 2006, the Legislature of the Commonwealth of Puerto Rico approved Act No. 117 (“Act 117”), which amends the Puerto Rico Internal Revenue Code of 1994 to provide for a sale and use tax of 5.5% to be imposed by the Commonwealth Government. Act 117 also authorizes each municipal government to impose a municipal sale and use tax of 1.5%. This municipal sales and use tax has in general the same tax base and limitations (except for unprocessed foods) as those provided by the Commonwealth’s sales and use tax.

Section 6189 of the Puerto Rico Internal Revenue Code of 1994, as amended, authorizes the Municipalities in Puerto Rico to impose a sales and use tax to consumers. This tax must be imposed in conformity with the base, exemptions and limitations contained Subtitle BB of the Code. The Municipal Sales Tax is specifically imposed over all sales transactions of taxable items and combined transactions (as defined by the municipal internal regulation) taken place within municipal limits. The Municipal Tax is also specifically imposed over the purchase price for the use, storage or consumption of taxable transactions (as defined by the municipal internal regulation) taken place within municipal limits.

The Municipal Legislature approved the imposition of the municipal sales and use tax, effective on July 1, 2006. Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. Tax is due each 20th day of each month based on tax collected in the preceding month. The Municipal Ordinance does not impose specific restrictions or limitations on the use of the municipal sales and use tax resources. Resources are recorded in the general fund of the Municipality.

NOTE 13 – INTERGOVERNMENTAL REVENUES

Intergovernmental revenues consist primarily of funds received from the Commonwealth of Puerto Rico, “in lieu of tax” payments from the Quasi-public Corporation, Puerto Rico Electric Power Authority, and federal financial assistance received from federal government. Grants and subsidies received from the Commonwealth of Puerto Rico and federal agencies include, among others, a general subsidy for urban development and capital improvements.

Intergovernmental revenues are accounted for through the General Fund except for those directly related to urban development and capital improvements, which are accounted for through the State Assignment, Sales Tax and Loans Funds.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 14 – EMPLOYEE'S RETIREMENT PLAN

The Employee's Retirement System of the Government of Puerto Rico and its instrumentality (ERS) is the administrator of a cost-sharing multiple-employer retirement system established by the Commonwealth of Puerto Rico. The ERS was created under the Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentality and of certain municipalities and components units not covered by their own retirement systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Head of Agencies and Public Instrumentality, Assistants of the Governor, the Comptroller of the Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees. ERS provides retirement, death and disability benefits. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

The Municipality adopted the requirements of GASBS No. 25 for all the career employees that are covered under the Commonwealth of Puerto Rico Employee's Retirement System, a multiple-employer public employee retirement system, established by State Laws.

Under the plan, the employees and employer portions are contributed, for which, the employee amount is withheld from salaries. Covered employees are required by Commonwealth statute to contribute 5.775% for the first \$550 of monthly salary plus 8.275% for the excess of this amount, or on the alternative, 8.275% of all salary. The Municipality contributes to the system 9.275% of the participating employee's salaries.

Law Number 305 of September 24, 1999, amends the Act Number 447 that establish a savings program. All employees active in the system as of December 31, 1999 may elect to transfer from define contribution programs to the new savings program (a defined contribution plan). Employees in the savings program may now contribute from a minimum of 8.275% up to a maximum of 10% of their monthly salary, and will invested in an account which will either: (a) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (b) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (c) earn a combination of both alternatives. If at time of retirement accumulated benefits amount to \$10,000 or less may elect to receive a lump sum distribution up to the accumulated benefits. Under the new program the retirement age is reduced from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

The pension benefit for participants who retire with less than 30 years of service is computed at the rate of 1½% of their average compensation for each year of credit service for the remaining years. The System also provides for death and disability benefits and the assets of the System pertaining to the participant employees.

A variety of significant actuarial assumptions are used to determine the standard measure of the pension benefit obligation and these assumptions are summarized below:

- ❖ The present value of the future pension payments was computed by using a discount of 9%.
- ❖ Future pension payments reflect an assumption of a 6% salary increase.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 14 – EMPLOYEE’S RETIREMENT PLAN (CONTINUED)

All employees that do not elect to transfer for the new program and who at the time of employment are 55 years old or less are eligible to participate in the System. Pension benefits for participants with 30 years of service are as follows:

<u>YEARS OF SERVICE</u>	<u>PARTICIPANT’S AGE</u>	<u>PENSION BENEFITS</u>
30 or more	55 or less	65% of the average of the three years of highest salary during the employee’s service period.
30 or more	58 or more	75% of the average of the three years of highest salary during the employee’s service period.
30 or more	65 or more	75% of the average of the three years of highest salary during the employee’s service period (employees started working after April 1, 1990).

The amount of the total pension benefit obligation is based on a standardized measurement established by GASBS No. 27, *Financial Reporting for Defined Benefit Pension Plans and Notes Disclosure for Defined Contributions Plans*. The standardized measurement is the actuarial present value of estimated defined pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee services performed to date. The measure is intended to help users assess the System’s funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among other public retirement systems. The measure is independent of the actuarial funding method used to determine contributions to the plan.

The membership of retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits, but not yet receiving benefits, and active employees and the distribution of active employees between vested and non-vested is not readily available.

Contributions in 2006 and prior years were made based on percentages established by the law. Such percentage has not been based on actuarial studies, as required by accounting principles generally accepted in the United States of America. An actuarial compilation of the annual contribution applicable to the Municipality has not been prepared. Accordingly, the accounts by which the actual contributions differ from the required actuarial contributions are not known.

The total pension expenditures recorded in the category of administration for the Fiscal Year Ended June 30, 2012 was approximately \$114,039. All employees who at the time of employment are 55 years old or less are eligible to participate in the System. No benefit is payable if the participant receives a refund of his accumulated contributions.

The historical trend information regarding the accumulation of assets and pension benefit obligation in the ERS is not available. For the ten-year trend information, refer to the separately issued financial statements of the ERS as of and for the fiscal year ended June 30, 2012. The P.R. Retirement Plan Administration provides additional information of the ERS. They issue a public available financial report that includes financial statements and required supplementary information for ERS, as a component unit of the Commonwealth of Puerto Rico. That report may be obtained by writing to the Administration at PO Box 42003, Minillas Station, San Juan, P.R. 00940.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 15 – CONTINGENCIES

A. CLAIMS AND JUDGMENTS

The Municipality is, at present, a defendant in a number of legal claims amounting to \$1.2 millions that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities.

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.

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in discovery stage. Certain of these claims are covered by insurance. Legal counsels with the information currently available can not determine the final outcome of these proceeding. However, it has been the Municipality's experience that such actions are settled for amounts substantially less than the claim amounts.

B. FEDERAL GRANTS

In the normal course of operations, the Municipality receives grants from various Federal and State agencies. The grant programs are subject to audit by agents of the granting authority, the purpose of which is to ensure compliance with conditions precedent to the granting of funds. Any liability for reimbursement, which may arise as the result of these audits is not believed to be material.

C. CONSTRUCTION

The Municipality had commitments at June 30, 2012 of approximately \$1,000,000 for the construction, improvements, or renovation of several capital facilities and the capital assets.

D. OTHER COMMITMENTS

At June 30, 2012 the General Fund had commitments of approximately \$219,522 for executory purchase orders or contracts that will be honored during the subsequent year.

NOTE 16 – FUND BALANCE

As of June 30, 2012, the fund balance (deficit) classifications are as follows:

Fund Balance	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Fund	Total
Restricted for:					
Public Safety	\$ -	-	-	35	35
Human Services and Welfare	-	-	-	8,533	8,533
Urban Development	-	2,652,620	-	26,012	2,678,632
Education	-	-	-	50,673	50,673
Debt Service	-	-	1,503,756	-	1,503,756
Assigned for:					
Human Services and Welfare	198,575	-	-	-	198,575
Urban Development	1,693,175	-	-	-	1,693,175
Unassigned	<u>(1,089,043)</u>	-	-	-	<u>(1,089,043)</u>
Total Fund Balance	<u>\$ 802,707</u>	<u>2,652,620</u>	<u>1,503,756</u>	<u>85,253</u>	<u>5,044,336</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

NOTE 17 – ACCOUNTING CHANGES AND RESTATEMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

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

Description	General Fund	State Assignment Fund	Loans Fund	Sales Tax Fund	Debt Service Fund	Other Governmental Funds	Totals
Fund balance, beginning	\$ (703,746)	3,136,140	326,558	627,096	1,163,769	84,788	4,634,605
To adjust interfund balances	367,258	(178,896)	(326,558)	-	-	-	(138,196)
Major fund reclassification	<u>627,096</u>	-	-	<u>(627,096)</u>	-	-	-
Fund balance, beginning as restated	<u>\$ 290,608</u>	<u>2,957,244</u>	<u>-</u>	<u>-</u>	<u>1,163,769</u>	<u>84,788</u>	<u>4,496,409</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:

Description	Total
Net assets, beginning	\$ 7,724,954
To eliminate interfund receivables	<u>(138,196)</u>
Net assets, beginning as restated	<u>\$7,586,758</u>

NOTE 18 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through April 30, 2013, which is the date the financial statements were available to be issued and determined that no material subsequent events require an estimate to be recorded or disclosed as of June 30, 2012.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with</u>
	<u>Original</u>	<u>Final</u>	<u>(Budgetary Basis)</u> <u>(See Note A)</u>	<u>Final Budget</u> <u>Positive</u> <u>(Negative)</u>
REVENUES:				
Property taxes	\$ 408,320	408,320	408,319	(1)
Volume of Business Taxes	165,379	165,379	150,008	(15,371)
Intergovernmental Revenues	2,726,441	2,726,441	2,666,208	(60,233)
Licenses, permits and other local taxes	351,587	351,587	239,322	(112,265)
Rent of Property	26,312	26,312	18,762	(7,550)
Miscellaneous	684,378	684,378	126,220	(558,158)
Prior Year Allocation	-	200,000	-	(200,000)
Total revenues	<u>4,362,417</u>	<u>4,562,417</u>	<u>3,608,839</u>	<u>(953,578)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
Mayor and Municipal Legislature	666,591	707,298	615,901	91,397
General Government	2,177,739	2,248,246	1,876,017	372,229
Public Safety	202,613	202,613	138,422	64,191
Public Works	557,510	612,748	515,016	97,732
Culture and Recreation	187,511	204,011	180,564	23,447
Sanitation	288,085	296,085	336,057	(39,972)
Human Service and Welfare	282,368	291,416	242,028	49,388
Total expenditures, encumbrances and other financing uses	<u>4,362,417</u>	<u>4,562,417</u>	<u>3,904,005</u>	<u>658,412</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	<u>\$ -</u>	<u>-</u>	<u>(295,166)</u>	<u>(295,166)</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTE TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

**NOTE A – EXPLANATION OF DIFFERENCE BETWEEN BUDGETARY INFLOWS AND
OUTFLOWS AND GAAP REVENUES AND EXPENDITURES**

Explanation of Differences:

Sources/inflows of resources:

Actual amounts (budgetary basis)“available for appropriation” from the budgetary comparison schedule	\$3,608,839
Differences-budget to GAAP:	
Prior and current GAAP adjustments to revenues	1,200,817
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$4,809,656</u>

Uses/outflows of resources:

Actual amounts (budgetary basis)“total charges to appropriations” from the budgetary comparison schedule	\$3,904,005
Differences-budget to GAAP:	
Prior Year expenditure are not outflows of budgetary resources but are expenditure for financial purposes	45,548
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(219,522)
GAAP adjustment to expenditures	<u>569,701</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$4,299,732</u>



NIEVES VELAZQUEZ & CO., P.S.C.

Certified Public Accountants and Financial Consultants

**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
Municipal Legislative Body
Municipality of Culebra
Culebra, Puerto Rico

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Municipality of Culebra, Puerto Rico, as of and for the year ended June 30, 2012, which collectively comprise the Municipality of Culebra, Puerto Rico's basic financial statements and have issued our report thereon dated April 30, 2013. We expressed an adverse opinion on the financial position of the governmental activities at June 30, 2012 and the related change in financial position for the year then ended due to several GAAP departures. 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

Management of the Municipality is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Municipality'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's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over financial reporting.

A deficiency in internal control 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 and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to (as items 12-II-1 and 12-II-2) be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies. (Items 12-II-3 and 12-II-4)

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies, or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain 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 instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as items 12-II-1, 12-II-2, 12-II-3 and 12-II-4.

We noted certain other matters that we reported to management of Municipality of Culebra in a separate letter dated April 30, 2013.

The Municipality of Culebra'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's response and, accordingly, we express no opinion on it.

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

San Juan, Puerto Rico
April 30, 2013

Nieves Velazquez & Co., P.S.C.

Stamp No. 2672778 of the Puerto Rico Society
Of Certified Public Accountants was
Affixed to the record copy of this report.





NIEVES VELAZQUEZ & CO., P.S.C.

Certified Public Accountants and Financial Consultants

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE
A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

To the Honorable Mayor and
Municipal Legislative Body
Municipality of Culebra
Culebra, Puerto Rico

Compliance

We have audited Municipality of Culebra compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have direct and material effect of the Municipality's major federal programs for the year ended June 30, 2012. The Municipality of Culebra 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 Municipality's management. Our responsibility is to express an opinion on Municipality's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; 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 Municipality of Culebra 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 Municipality of Culebra compliance with those requirements

As described in item(s), 12-III-1 and 12-III-2 in the accompanying schedule of findings and questioned costs, Municipality of Culebra, did not comply with requirements that are applicable to its Compliance with such requirements is necessary, in our opinion, for Municipality of Culebra, to comply with the requirements applicable to that program.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE
A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133
(Continued)**

In our opinion, except for the noncompliance described in the preceding paragraph, Municipality of Culebra, complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal program for the year ended June 30, 2012. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 12-III-3, 12-III-4 and 12-III-5.

Internal Control Over Compliance

Management of Municipality of Culebra, 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 Municipality of Culebra's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 Culebra's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of finding and questioned costs as items 12-III-1 and 12-III-2 to be material weaknesses.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE
A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

(Continued)

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 12-III-3, 12-III-4 and 12-III-5 to be a significant deficiency.

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

This report is intended solely for the information and use the management, City Council, others within the entity, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

San Juan, Puerto Rico
April 30, 2013

Nieves Velazquez & Co., P.S.C.

Stamp No. 2672779 of the Puerto Rico Society
of Certified Public Accountants was affixed
to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2012**

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number (Note 2)</u>	<u>Pass-through Entity Identifying Number (Note 3)</u>	<u>Federal Expenditures (Notes 1 and 4)</u>
<u>U.S. Department of Agriculture</u>			
Direct Programs:			
Rural Business Enterprise Grants	10.769	Not Available	\$ 51,916
Pass-Through the Commonwealth of Puerto Rico – Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	<u>21,882</u>
Total U.S. Department of Agriculture			<u>73,798</u>
<u>U.S. Department of Housing and Urban Development</u>			
Indirect Programs:			
Pass-Through State – Office of the Commissioner of Municipal Affairs:			
Community Development Block Grants – State's Program	14.228	Various	436,200
Community Development Block Grants – State Program (Recovery Act Funded)	14.255	08-AB-AR-002	<u>21,823</u>
Total Community Development Block Grants – Cluster			<u>458,023</u>
Pass-Through State – State Department of Family:			
Homelessness Prevention and Rapid Re-Housing Program (Recovery Act Funded)	14.257	Not Available	<u>5,703</u>
Total U.S. Department of Housing and Urban Development			<u>463,726</u>
<u>U.S. Department of Health and Human Service</u>			
Pass-Through State - Office of Governor, Regional Elderly Office:			
Special Program for Aging, Title III, Part B	93.045	Not Available	<u>12,686</u>
Pass-Through State - Administration for Children and Families:			
Child Care and Development Block Grant	93.575	Not Available	<u>147,975</u>
Total U.S. Department of Health and Human Service			<u>160,661</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$698,185</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2012**

1. GENERAL

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Culebra, Puerto Rico (Municipality) and is presented on the modified accrual basis. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Government and Nonprofit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the governmental funds financial statements. The reporting entity is defined in Note 1 (A) to the governmental funds financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying Schedule of Expenditures of Federal Awards is prepared from Municipality's accounting records and is not intended to present financial position or the results of operations. The Municipality in accordance with the terms records the financial transactions and conditions of the grants, which are consistent with accounting principles generally accepted in the United States of America. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable or when actually paid, whichever occurs first.

3. FEDERAL CFDA NUMBER

The CFDDA numbers included in this Schedule are determined based on the program name, review of grant contract information and the Office of Management and Budget's Catalogue of Federal Domestic Assistance.

4. PASS-THROUGH GRANTOR'S NUMBER

State or local government redistributions of federal awards to the Municipality, treated as if they were received directly from the federal government. OMB Circular A-133 requires the Schedule to include the name of the pass-through entity and identifying number assigned by the pass-through entity for federal awards received as a sub-recipient. Numbers identified as N/AV are not available.

5. MAJOR PROGRAM

Major program is identified in the Summary of Auditor's Results of the Schedule of Findings and Questioned Costs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2012

6. RECONCILING OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE GOVERNMENTAL FUNDS FINANCIAL STATEMENT

Amounts included in the accompanying schedule agree with the amounts included in the basic financial statements as follows:

<u>Fund</u>	<u>Federal Assistance</u>	<u>Other Assistance</u>	<u>Financial Statements</u>
Other Governmental Funds	<u>\$698,185</u>	<u>144,970</u>	<u>843,155</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section I. Summary of Audit Results

Part I. Financial Statements

- | | | | |
|----|---|--------------------|--------------|
| 1. | Type of audit report issued – Governmental Activities | Adverse | |
| 2. | Internal control over financial reporting: Mayor funds and aggregate remaining fund information | Unqualified | |
| | ❖ Material weakness (es) identified? | <u> </u> Yes | <u> </u> No |
| | ❖ Significant deficiency (ies) identified? | <u> </u> Yes | <u> </u> No |
| 3. | Noncompliance material to financial statement noted? | <u> </u> Yes | <u> </u> No |

Part II. Federal Awards

- | | | | |
|----|--|------------------|--------------|
| 1. | Internal control over major programs: | | |
| | ❖ Material weakness (es) identified? | <u> </u> Yes | <u> </u> No |
| | ❖ Significant deficiency (ies) identified? | <u> </u> Yes | <u> </u> No |
| 2. | Type of auditors report issued on compliance for major programs: | Qualified | |
| 3. | Any audit findings disclosed that are required to be reported in accordance with 510(a) of OMB Circular A-133? | <u> </u> Yes | <u> </u> No |
| 4. | Identification of major programs: | | |

Name of Federal Program or Cluster

CFDA Number (s)

- | | | |
|----|---|----------------------------|
| 5. | Community Development Block Grant | 14.228 |
| | ARRA Community Development Block Grant | 14.255 |
| 5. | Dollar threshold used to distinguish between Type A and Type B programs | \$300,000 |
| 6. | Auditee qualified as low-risk auditee? | <u> </u> Yes <u> </u> No |

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section II.	Financial Statement Findings
FINDING	12-II-1
REQUIREMENT	SIGNIFICANT DEFICIENCIES OVER PROPERTY, PLANT AND EQUIPMENT
CONDITION	The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net assets, and expenses of the governmental activities is not determinable. This finding is repeated from prior years.
CRITERIA	Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain updated property accounting records. Also, the GASB Statement No. 34 requires that all capital assets, including infrastructure, must be presented in the Statement of Net Assets and that these assets must be depreciated during its useful life.
CAUSE	Competent and sufficient evidential matter related to the capital assets was not available to support the value, completeness and ownership of these capital assets.
EFFECT	The Municipality's Government Wide Financial Statements do not present fairly, the financial position of the governmental activities, and the change in net assets of the Municipality.
RECOMMENDATION	We recommend that the Municipality should continue the compilation of documents to support the value, completeness and ownership of its capital assets, to comply with the requirements of the GASB Statement No. 34.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76 – 81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section II. Financial Statement Findings

FINDING **12-II-2**

CATEGORY **INTERNAL CONTROLS**

TOPIC SENTENCE **ACCOUNTING SYSTEM**

CONDITIONS The accounting system and manuals used by the Municipality to account and register the financial transactions during the fiscal year does not provide for the summarization of transactions that permit the preparation of Municipality's financial statements in conformity with the General Accepted Accounting Principles of the United States of America (GAAP). This finding is repeated from prior year.

CRITERIA According to Article 8.010(a) and (b) of Law Num. 81 for the Municipalities of Puerto Rico, the computerized system and the procedures of accounting and property will be design so that it allows the Municipality to carry out its functions, at the same time as they serve to maintain an uniform and coordinated accounting, that provide a complete picture of the financial operations of the Municipality and the necessary financial information that assist the Municipality Legislature, the Governor, and the Secretary of the Puerto Rico Treasury Department in the performance of its respective responsibilities. Municipalities accounting will be based on funds, Generally Accepted Accounting Principles and the requirements established by the Governmental Accounting Standard Boards.

CAUSE Municipality's accounting system and financial reports are subject to State's agencies requirements, which does not allow nor provide the Municipality with the necessary tools capable of recapturing the financial information and provide financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section II. Financial Statement Findings

FINDING 12-II-2 (Continuation)

EFFECT The lack of an adequate accounting system which can captures all the financial information and generates Municipality's financial statements for each fiscal year affect the Municipality ability to measure the financial and non-financial performance of programs and activities; adequately safeguard significant assets and properly record various transactions; and hinder the Municipality from having reliable financial information to operate in an economical, efficient, and effective manner.

Sound decisions on the current results and future direction of vital programs and policies are made more difficult without timely, reliable and useful financial performance information.

RECOMMENDATION The Municipality should establish and implement the necessary measures that allow the summarization of the financial transactions in order to prepare the financial statements in conformity with GAAP.

QUESTIONED COSTS None

MANAGEMENT RESPONSE See Corrective Action Plan attached to this report (pages 76 – 81).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012

Section II.	Financial Statement Findings
FINDING	12-II-3
REQUIREMENT	MUNICIPAL SOLID WASTE LANDFILL – GASB 18
CONDITION	The Municipality has not maintained complete and adequate records in order to obtain, competent evidential matter with respect to closure and post-closure cost of the municipal solid waste landfill.
CRITERIA	The Governmental Accounting Standards Statement No. 18, Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Cost require that the Municipality maintain adequate accounting records to support the estimated closing and post closing care cost.
CAUSE	The Municipality does not have the resources to determine the required closing and post closing care cost of it landfill.
EFFECT	The accountants report on the Statement of Activities and Net Assets is an adverse opinion.
RECOMMENDATION	We recommend the Municipality to hire an external professional source to determine the closing and post closing care cost to comply with GASB No. 18.
QUESTIONED COST	None
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Section II – Financial Statement Findings

FINDING	12-II-4
REQUIREMENT	Supporting Payment Documents
CONDITIONS	During our disbursement test for Rural Development Project “Market Place”, we noted that the supporting documents for a payment of \$51,847 could not be located by the municipality officials and, therefore, could not be examined by us.
CRITERIA	Chapter XVI, Article 16.014 of State Act Number 81 of August 30, 1991 states that the Municipality should assign an accountant to maintain proper accounting records including supporting payment documentations.
CAUSE	The designated accountant has not maintained proper and updated accounting records.
EFFECT	The Municipality officials could be issuing checks without the required supporting documentation.
QUESTIONED COSTS	Cost of \$51,847 is questioned.
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section III – Federal Award Findings and Questioned Costs

FINDING	12-III-1
CATEGORY	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
REQUIREMENT	Compliance and Internal Control
NONCOMPLIANCE	Equipment and Real Property Management
CONDITIONS	Federal Program Department does not have a property register that includes all the required information; it only includes the property number and its description. Also, no physical inventory has been taken in the last two years.
CRITERIA	Subpart C, 24 CFR 85.32 (d)(1), states that property records must be maintained and its shall includes: a description of the property, serial number or other identification number, the source of property, percentage of Federal participation in the property, the location, use and condition of the property, any ultimate disposition data including the date of disposal and sales price of property. Also, a physical inventory of the property must be taken and the result reconciled with the property records at least on every two years, respectively.
CAUSE	The Municipality does not maintain the appropriate information on the real property records to assure that it is in accordance with the federal regulation.
EFFECT	The Municipality is not in compliance with Subpart C, 24 CFR 85.32 (d)(1).
RECOMMENDATION	The Municipality should revise and update its property records according to the federal regulation.
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section III – Federal Award Findings and Questioned Costs

FINDING	12-III-2
CATEGORY	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
REQUIREMENT	Compliance
NONCOMPLIANCE	Suspension and Debarment
TOPIC SENTENCE	Lack of Control Over Suspension and Debarment
CONDITIONS	<p>The Municipality does not have procedures in place to verify the status of an entity as to suspensions and debarments when contracting services or procuring goods with federal funds.</p> <p>In testing procurement, suspension and debarments, we were not able to find evidence indicating that the Municipality performs procedures to assure that the individuals and entities that receive contracts or sub-awards are not suspended or debarred from participation in federal programs. For example, we found an instance where municipality official could not provide the contract file that contain the request for proposals, bid, evaluations and other related documents and to be examined by us.</p>
CRITERIA	<p>As stated in 24 CFR 85.35 grantee and sub-grantee must not make any award or permit any award (sub-grant or contract) at any tier to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in Federal Assistance Program under Executive Order 12549, "Debarment and Suspension". Also, A-102 Common Rule (.36) contains the procurement requirements that should be followed to obtain competitive contract price for the service and/or materials to be acquired.</p>
CAUSE	<p>The Municipality has no policies and procedures for the use of the list of parties excluded from federal procurement or non-procurement programs to assure that they do not award assistance to listed parties.</p>
EFFECT	<p>As a result of this deficiency, the Municipality could have procured goods or services from organizations and individuals that are suspended or debarred which could result in cost disallowances by the federal awarding agency.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section III – Federal Award Findings and Questioned Costs

FINDING	12-III-2 (Continued)
CATEGORY	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
RECOMMENDATION	The Municipality should amend their procurement procedures and include a step to verify whether or not the individual or entity is on the list or parties excluded from federal participation in procurement and non-procurement programs. The Municipality should also require the entities or individuals to submit a certification stating that they are not suspended or debarred.
QUESTIONED COSTS	NONE
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section III – Federal Award Findings and Questioned Costs

FINDING	12-III-3
CATEGORY	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
REQUIREMENT	Compliance and Internal Control
NONCOMPLIANCE	Cash Management
CONDITIONS	The program does not maintain proper procedures to minimize time elapsing between funds received and disbursed.
CRITERIA	The Cash Management General Requirement of Circular OMB-102 requires that funds should include procedures to minimize the time elapsed between the transfer of funds from the U.S. Treasury (Pass-through State – Office of Commissioner of Municipal Affairs) and the disbursement and cash receipts we found three instances out of 4 examined that the disbursements were made elapsing between 8 to 14 days. This finding is repeated from prior years.
CAUSE	The program officials does not follow up when funds are received to disburse them immediately.
EFFECT	The Municipality is not in compliance with the Circular OMB-102 Cash Management Requirement.
RECOMMENDATION	We recommend the Municipality officials to implement and/or improve its cash management procedures to comply with the requirement.
QUESTIONED COSTS	NONE
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012

Section III – Federal Award Findings and Questioned Costs

FINDING	12-III-4
CATEGORY	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
REQUIREMENT	Compliance
NONCOMPLIANCE	Reporting
CONDITIONS	During our Test of Reporting we found one quarterly report (4/12-6/30/12) filed 26 days after the due date and for the other three quarterly report no submission evidence was provided.
CRITERIA	Performance and Evaluation Report (OMB No. 2506-0085) – This report is due from each State CDBG grantee within 90 days after the close of its program year in a format suggested by HUD. HUD encourages the submission of the report in both paper and computerized formats. Among other factors, the report is to include a description of the use of funds during the program year and an assessment of the grantee's use for the priorities and objectives identified in its plan.
CAUSE	Most of these reports are submitted by certified mail but, the certified receipts is not attached to the report office copy an, therefore, the submission date is not known.
EFFECT	The late submissions of such reports may cause an improper hand ling of amounts been expensed and obligated..
RECOMMENDATION	We recommend that each report copy submitted should be identified and the certified receipt be attached immediately to the report office copy.
QUESTIONED COSTS	NONE
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2012**

Section III – Federal Award Findings and Questioned Costs

FINDING	12-III-5
CATEGORY	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
REQUIREMENT	Compliance
NONCOMPLIANCE	Period of Availability of Federal Funds
CONDITIONS	During our Test of Availability of Federal Funds we noted that funds pertaining to year 2008 and amounting to \$138,146 were not obligated within the 24 months period required.
CRITERIA	The OMB Circular A-133, establishes federal awards may specify a time period during which the non-federal entity may use the federal funds. Where a funding period is specified, a non-federal entity may charge to the award only costs resulting from obligations incurred during the funding period and any pre-award costs authorized by the federal awarding agency. The period to obligate the award is 24 months and the period to expense is 4 years.
CAUSE	The Municipality officials are not monitoring the funding period to ascertain that program fund are obligated and expensed within the 24 months and 4 years period, respectively.
EFFECT	The assigned funds are not used completely within the time frame requirement and therefore, could be lost.
RECOMMENDATION	We recommend that the Municipality officials should plan and evaluate the use of such funds on time and to strengths its procedures and internal control to avoid possible lost of such funds. We also recommend to request an approval from HUD to reprogram those funds.
QUESTIONED COSTS	NONE
MANAGEMENT RESPONSE	See Corrective Action Plan attached to this report (pages 76-81).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III - Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2011	All Programs	II-II-1	<p>Property, Plant and Equipment</p> <p>Criteria and Condition:</p> <p>Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain updated property accounting records. Also, the GASB Statement No. 34 requires that all capital assets, including infrastructure, must be presented in the Statement of Net Assets and that these assets must be depreciated during its useful life.</p> <p>The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net assets, and expenses of the governmental activities is not determinable. This finding is repeated from prior years.</p>	Finding repeated in the current year. (12-II-1)
06/30/2011	All Programs	II-II-2	<p>Accounting System</p> <p>Criteria and Condition:</p> <p>According to Article 8.010(a) and (b) of Law Num. 81 for the Municipalities of Puerto Rico, the computerized system and the procedures of accounting and property will be design so that it allows the Municipality to carry out its functions, at the same time as they serve to maintain an uniform and coordinated accounting that provide a complete picture of the financial operations of the Municipality and the necessary financial information that assist the Municipality Legislature, the Governor, and the Secretary of the Puerto Rico Treasury Department in the performance of its respective responsibilities. Municipalities accounting will be based on funds, Generally Accepted Accounting Principles and the requirements established by the Governmental Accounting Standard Boards.</p>	Finding repeated in current year. (See 12-II-2)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III - Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2011	All Programs	11-II-2	<p>Accounting System (Continuation)</p> <p>Criteria and Condition:</p> <p>The accounting system and manuals used by the Municipality to account and register the financial transactions during the fiscal year does not provide for the summarization of transactions that permit the preparation of Municipality's financial statements in conformity with the General Accepted Accounting Principles of the United States of America (GAAP). This finding is repeated from prior year.</p>	
06/30/2011	All Programs	11-II-3	<p>Municipal Solid Waste Landfill – GASB 18</p> <p>Criteria and Condition:</p> <p>The Governmental Accounting Standards Statement No. 18, Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Cost require that the Municipality maintain adequate accounting records to support the estimated closing and post closing care cost.</p> <p>The Municipality has not maintained complete and adequate records in order to obtain, competent evidential matter with respect to closure and post-closure cost of the municipal solid waste landfill.</p>	Finding repeated in the current year. (See 12-II-3)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III - Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2011	CDBG	III-1	<p>Equipment and Real Property Management</p> <p>Criteria and Condition:</p> <p>Subpart C, 24 CFR 85.32 (d)(1), states that property records must be maintained and its shall includes: a description of the property, serial number or other identification number, the source of property, percentage of Federal participation in the property, the location, use and condition of the property, any ultimate disposition data including the date of disposal and sales price of property. Also, a physical inventory of the property must be taken and the result reconciled with the property records at least on every two years, respectively.</p> <p>Federal Program Department does not have a property register that includes all the required information; it only includes the property number and its description. Also, no physical inventory has been taken in the last two years.</p>	Finding repeated in the current year. (12-III-1)
06/30/2010	CDBG	III-2	<p>Lack of Control Over Suspension and Debarment</p> <p>Criteria and Condition:</p> <p>As stated in 24 CFR 85.35 grantee and sub-grantee must not make any award or permit any award (sub-grant or contract) at any tier to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in Federal Assistance Program Under Executive Order 12549, "Debarment and Suspension".</p> <p>The Municipality does not have procedures in place to verify the status of an entity as to suspensions and debarments when contracting services or procuring goods with federal funds.</p> <p>In testing procurements, suspension and debarments, we were not able to find evidence indicating that the Municipality performs procedures to assure that the individuals and entities that receive contracts or sub-awards are not suspended or debarred from participation if federal programs.</p>	Finding repeated in the current year. (12-III-2)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III - Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2011	CDBG	III-3	<p>Cash Management</p> <p>Criteria and Condition:</p> <p>The Cash Management General Requirement of Circular OMB-102 requires that funds should include procedures to minimize the time elapsed between the transfer of funds from the U.S. Treasury (Pass-through State-Office of Commissioner of Municipal Affairs) and the disbursement elapsing between 10 to 68 days. This finding is repeated from prior years.</p> <p>The program does not maintain proper procedures to minimize time elapsing between funds received and disbursed.</p>	Finding repeated in the current year. (12-III-3)
06/30/2010	CDBG	4-10	<p>Equipment and Real Property Management</p> <p>Criteria and Condition:</p> <p>Subpart C, 24 CFR 85.32 (d)(1), states that property records must be maintained and its shall includes: a description of the property, serial number of other identification number, the source of property, percentage of federal participation in the property, the location, use and condition of the property, any ultimate disposition data including the date of disposal and sales prices of property. Also, a physical inventory of the property must be taken and the result reconciled with the property records at least on every two years, respectively. The Municipality does not have a property register that includes all the required information; it only includes the property number and its description.</p>	Finding repeated in the current year. (12-III-1)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III - Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2010	CDBG	5-10	<p>Procurement Suspension and Debarment</p> <p>Criteria and Condition:</p> <p>States, and governmental sub-recipients of States, shall use the same State policies and procedures used for procurements from non-federal funds. They also shall ensure that every purchase order or other contract includes any clauses required by Federal statutes and executive order and their implementing regulations.</p> <p>Local governments and Indian tribal governments which are not sub-recipients of States will use their own procurements procedures provided that they conform to applicable Federal Law and Regulations and standards identified in the A-102 Common Rule.</p> <p>All non-federal entities shall follow Federal laws and implementing regulations applicable to procurements as noted in Federal agency implementation of the A-102 Common Rule and OMB Circular 2 CFR, Part 180 states that non-federal entities are prohibited from contracting with or making sub-awards under covered transactions to parties that are suspended or debarred or whose principals are suspended or debarred. Covered transactions include those procurement contracts for goods and services awarded under a non-procurement transaction (e.g., grant or cooperative agreement) that are expected to equal or exceed \$25,000 or meet certain other specified criteria. CFR, Section 180.220 of the government-wide non-procurement debarment and suspension guidance contains those additional limited circumstances. All non-procurement transactions (i.e., sub-awards to sub-recipients), irrespective of award amount, are considered covered transactions.</p>	Finding repeated in the current year. (12-III-2)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III. Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2010	CDBG	5-10	<p>Procurement Suspension and Debarment (Continuation)</p> <p>Criteria and Condition:</p> <p>When a non-federal entity enters into a covered transaction with an entity at a lower tier, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded. This verification may be accomplished by checking the Excluded Parties List System (EPLS) maintained by the General Services Administration (GSA), collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity.</p> <p>As part of the audit procedures the prior auditor examined 14 disbursements to test the compliance with the Procurement and Suspension and Debarment requirement for Community Development Block Grant program. In 10 of the 14 disbursements amounting \$919,712.44, the Municipality did not comply with Suspension and Debarment requirement and in one disbursement amounting to \$27,900 the Municipality did not comply with the procurement requirement.</p>	
06/30/2010	CDBG	6/10	<p><u>Davis-Bacon Act</u></p> <p>Criteria and Condition:</p> <p>Section 40 USC 3141-3144, 346 and 347 state that when required by the Davis-Bacon Act, the Department of Labor's (DOL) government wide implementation of the Davis-Bacon Act, or by Federal program legislation, all labor and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by Federal Assistance Fund must be paid wages not less than those established for the locality of the project (prevailing wage rate) by the DOL.</p>	Finding did not occur in the most current two years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2012**

Section III. Federal Award Findings and Questioned Costs

<u>Single Audit Report</u>	<u>Program</u>	<u>Finding No.</u>	<u>Finding</u>	<u>Current Status</u>
06/30/2010	CDBG	6-10	<p><u>Davis-Bacon Act (Continuation)</u></p> <p>Criteria and Condition:</p> <p>Non-federal entities shall include in their construction contracts subject to the Davis-Bacon Act a requirement that the contractor or subcontractor comply with the requirements of the Davis-Bacon Act and the DOL regulations (29 CFR, Part 5, "Labor Standards Provisions Applicable to Contracts Governing Federally Financed and Assisted Construction"). This includes a requirement for the contractor or subcontractor to submit to the non-federal weekly, for each week in which any contract.</p> <p>Weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payrolls) (29 CFR, Section 5.5 and 5.6). This reporting is often done using Optional Form WH-247, which includes the required statement of compliance (OMB No. 1215-0149).</p> <p>As part of the audit procedures the prior auditor tested 14 disbursements to the test the compliance with the Davis-Bacon Act for Public Assistance Grants Program. In 2 of the 8 the contractors did not submit the payrolls to the Municipality for examination</p>	
06/30/2010	CDBG	7-10	<p><u>Reporting</u></p> <p>Criteria and Condition:</p> <p>Memorandum Circular OCAM-1994 requires that the quarterly reports should be received in the agency the last day of the subsequent month to the quarter end. The Municipality did not provide the prior auditor to examination the quarterly report of January to March 2010.</p>	Finding occurred in the current year.
06/30/2010	CDBG	8-10	<p><u>Cash Management</u></p> <p>Criteria and Condition:</p> <p>Memorandum Circular OCAM-2009-21 requires that opening a different bank account to the CDBG funds from the deposit of the funds assigned for ARRA funds.</p>	Finding repeated in the current year. (12-III-3)



CORRECTIVE ACTION PLAN SINGLE AUDIT 2011-2013

Financial Statements Findings

Finding 12-II-1- Property, Plant and Equipment

The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net assets, and expenses of the governmental activities is not determinable.

Corrective Action

The Finance Department Director will give instructions to the Property Division of the Municipality to continue updating its capital assets inventory. Once the inventory is updated we will create a subsidiary record which will include the description of the assets, the person in charge of the assets, the date of acquisition and the cost. Also, the subsidiary will include the accumulated depreciation, the depreciation expense and the book value of the capital assets, in order to comply with the GASB 34. In addition, we will consider taking the Municipality's infrastructure inventory.

Responsible Person

Frank García Martínez

12-II-2- Accounting System

The accounting system and manuals used by the Municipality to account and register the financial transactions during the fiscal year does not provide for the summarization of transactions that permit the preparation of Municipality's financial statements in conformity with the General Accepted Accounting Principles of the United States of America (GAAP).

Corrective Action

The Municipality maintains two set of accounting records; a manual system and the computerized, provided by the Office of Commissioner of Municipal Affairs (OCAM). The manual system is the one we are using for financial reporting and the preparation of financial statements. This system consists of a set of manual books (Excell spreadsheets) which are used to register all the sources of revenues, expenditures, encumbrances and the budget of the Municipality. During the fiscal year 2013-2014 we are going to make various changes and improvements to this manual accounting system. The computerized system that maintained the Municipality is used only to prepare the purchases orders and the checks of the General Fund. In the meanwhile, we will continue with this practice until we acquire new accounting software that can resolve this condition.

Responsible Person

Frank García Martínez

12-II-3- Municipal Solid Waste Landfill

The Municipality has not maintained complete and adequate records in order to obtain, competent evidential matter with respect to closure and post-closure cost of the municipal solid waste landfill.

Corrective Action

The Municipality will request a confirmation from the State Solid Waste Authority of the available space, if any, of the municipal solid waste landfill. Once we obtain that information we will hire an external professional to determine the actual closure and post-closure care cost of the landfill. With that information we will proceed to calculate the required liability for the financial statements of the Municipality, of the closure and post-closure costs of the landfill.

Responsible Person

Frank García Martínez

12-II-4- Supporting Payments Documents

During our disbursement test for Rural Development Project “Market Place”, we noted that the supporting documents for a payment of \$51,847 could not be located by the Municipality’s officials and, therefore, could not be examined by us.

Corrective Action

The Finance Department Director of the Municipality will gave the instructions, immediately to the employees, to find all the supporting documents that justified the disbursement in the amount of \$51,847 mentioned in this finding.

Responsible Person

Frank García Martínez

Federal Award Findings

12-III-1- Equipment and Real Property Management

Federal Program Department does not have a property register that includes all the required information; it only includes the property number and its description. Also, no physical inventory has been taken in the last two years.

Corrective Action

In order to correct this situation, we will review the property record in order to assure that include the following information: (1) a description of the property; (2) serial number or other identification number; (3) the source of property, percentage of federal participation in the property; (4) the location; (5) use and condition of the property; (6) any ultimate disposition data including the date of disposal, and; (7) sale price of property. Also, we will coordinate with the Property Division of the Municipality to take a physical inventory before the end of this fiscal year.

Responsible Person

Brenda Cruz Walker

12-III-2- Suspension and Debarment

The Municipality does not have procedures in place to verify the status of an entity as to suspensions and debarments when contracting services of procuring goods with federal funds.

In testing procurement, suspension and debarment, we were not able to find evidence indicating that the Municipality performs procedures to assure that the individuals and entities that receive contracts or subawards are not suspended or debarred from participation in federal programs. For example, we found an instance where municipality official could not provide the contract file that contains the request for proposals, bid, evaluations and other related documents and to be examined by us.

Corrective Action

To correct this situation, we will established during our procurement procedures, a step to verify through the electronic version available on the Internet whether or not the individual or entity is on the list of parties excluded from federal participation in procurement and non-procurement programs. Also, we will give instructions to the Federal Program Director to maintain evidence of all the documents related to bids or quotations that were paid with Federal funds.

Responsible Person

Brenda Cruz Walker

12-III-3- Cash Management

The program does not maintain proper procedures to minimize time elapsing between funds received and disburse.

Corrective Action

To avoid this situation we gave instructions to the Federal Program Director and the Finance Department, that once the funds from the pass-through are received, the checks has to be issue in approximately three (3) days.

Responsible Persons

Brenda Cruz Walker
Frank García Martínez

12-III-4- Reporting

During our Test of Reporting we found one quarterly report (4/12- 6/30/12) filed 26 days after the due date and for the other three quarterly report no submission evidence was provided.

Corrective Action

We gave instructions to the Federal Program's accountant to submit in a timely manner, to the pass-through entity the required reports. Also, the accountant should maintain and safeguard the evidence of the submissions of the reports to the pass-through entity.

Responsible Person

Brenda Cruz Walker

12-III-5- Period of Availability of Federal Funds

During our Test of Availability of Federal Funds we noted that funds pertaining to year 2008 and amounting to \$138,146 were not obligated within the 24 months period required.

Corrective Action

We will make an analysis of the available funds that we have in the pass-through entity and we will assure that those funds will be used during the period of availability to avoid the possible loss of funds.

Responsible Person

Brenda Cruz Walker

Responsible Officials,



William I. Solís Bermúdez
Mayor



Frank García Martínez
Finance Department Director



Brenda Cruz Walker
Federal Program Director