

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**



**BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION**

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION
FISCAL YEAR ENDED JUNE 30, 2013**

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

Certified Public Accountants and Financial Consultants

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor,
Members of the Municipal Legislature
and People of the 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 of the Commonwealth of Puerto Rico (the Municipality), as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

INDEPENDENT AUDITOR'S REPORT

(Continued)

Basis for Adverse Opinion on Governmental Activities

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 assets additions be capitalized and depreciated over their estimated useful lives, which would increase the assets, net position and expenses of the governmental activities. The amount by which this departure would affect the assets, net position 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 requirements 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. Environmental Protection Agency. At June 30, 2013, the accompanying statement of net position 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, 2013.

Adverse Opinion

In our opinion, because of the significance of the matters discussed in the "Basis for Adverse Opinion on Governmental Activities" paragraphs, the financial statements referred to previously do not present fairly the financial position of the governmental activities of the Municipality of Culebra of the Commonwealth of Puerto Rico, as of June 30, 2013, or the changes in financial position thereof for the year then ended.

Unmodified Opinions

In our opinion, the financial statements referred to above 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 of the Commonwealth of Puerto Rico, as of June 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT

(Continued)

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 17, 2014 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Municipality's internal control over financial reporting and compliance.

Other Matters

Required Supplementary Information

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 5 through 11 and 49 through 50, 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 inquiries 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 others 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

INDEPENDENT AUDITOR'S REPORT

(Continued)

Other Matters

Required Supplementary Information

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 in all material respects in relation to the financial statements as a whole.

Nieves Velazquez & Co., P.S.C.
NIEVES VELAZQUEZ & CO., P.S.C.

San Juan, Puerto Rico
February 28, 2014

CPA Stamp No. 02696602 was affixed
to the original of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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, 2013. 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, 2013 by \$8,110,173, and at June 30, 2012 by \$8,287,502;
- ❖ The Municipality's total net position decreased by \$177,329 during fiscal year 2012-2013;
- ❖ As of June 30, 2013, the Municipality's governmental funds reported combined ending fund balances of \$4,739,758, a decrease of \$304,578 from the prior year;
- ❖ At June 30, 2013, the unrestricted deficit was \$2,454,891.
- ❖ The Municipality's capital assets inventory had no movement during fiscal year;
- ❖ The investment in capital assets for this year was not determinable;
- ❖ Loans principal payments were \$50,000 and \$85,000 in 2013 and 2012, 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, 2013**

GOVERNMENT-WIDE FINANCIAL STATEMENTS (CONTINUED)

The Statement of Net Position presents information on all of the Municipality's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position 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 position changed during the most recent fiscal year. All changes in net position 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, 2013**

GOVERNMENT-WIDE FINANCIAL ANALYSIS

GOVERNMENTAL NET POSITION

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of the Municipality, assets exceeded liabilities by \$8,110,173 as of June 30, 2013 versus \$8,287,502, as of June 30, 2012. Our analysis below focuses on the net position (**Table 1**) and changes in net position of the Municipality's governmental activities.

Table 1		
Statement of Net Position	2013	2012
Current and non-current assets	\$ 5,654,810	\$ 5,664,513
Capital assets	8,412,866	8,412,866
Total Assets	14,067,676	14,077,379
Current liabilities	584,455	443,086
Long-term liabilities	5,132,531	5,183,681
Total Liabilities	5,716,986	5,626,767
Deferred Inflow of Revenues	240,517	163,110
Net position:		
Investment in capital assets, net of related debt	6,097,866	6,047,866
Restricted	4,467,198	4,241,629
Deficit	(2,454,891)	(2,001,993)
Total Net Position	\$ 8,110,173	\$ 8,287,502

The largest portion of the Municipality's net position 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 position represents resources that are subject to external restrictions on how they may be used.

GOVERNMENTAL ACTIVITIES

Governmental activities increased the Municipality's net position. Key elements of this increase are as follows: the Municipality's governmental activities had net expenses of \$5,691,476. 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 did not exceed net expenses by \$177,329.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

GOVERNMENT-WIDE FINANCIAL ANALYSIS (CONTINUED)

GOVERNMENTAL ACTIVITIES (CONTINUED)

The cost of all governmental activities this year was \$6,956,800. **Table 2** presents the cost of each of the Municipality's largest programs.

Table 2			
Statement of Activities		2013	2012
Revenues			
Grants and contributions	\$	1,265,324	\$ 890,947
General revenues:			
Property taxes		576,704	616,359
Volume of business taxes		157,136	150,008
Sales taxes		1,390,070	1,473,648
Intergovernmental		2,898,220	2,666,208
Rent		15,375	18,762
Licenses and permits		209,970	239,322
Miscellaneous		266,672	106,351
Total revenues		<u>6,779,471</u>	<u>6,161,605</u>
Expenses			
General government		3,106,042	2,470,743
Public safety		159,369	138,422
Public works		1,236,742	850,752
Culture and recreation		204,354	180,564
Human services and welfare		441,645	403,844
Urban development		1,536,980	1,187,488
Education		217,093	171,277
Interest on long-term debts		54,575	57,771
Total expenses		<u>6,956,800</u>	<u>5,460,861</u>
Changes in net position		(177,329)	700,744
Net position – beginning		8,287,502	7,586,758
Net position – ending	\$	<u>8,110,173</u>	\$ <u>8,287,502</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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	2013	2012	
Assets:			
Total assets – Major Funds	\$ 7,735,115	\$ 7,488,353	
Total assets – Other Funds	672,467	1,025,542	
Combined total assets	<u>8,407,582</u>	<u>8,513,895</u>	
Liabilities:			
Total liabilities – Major Funds	3,002,255	2,515,289	
Total liabilities – Other Funds	334,972	777,179	
Combined total liabilities	<u>3,337,227</u>	<u>3,292,468</u>	
Deferred Inflows of Resources:			
Total – Major Fund	90,080	13,981	
Total – Other Funds	240,517	163,110	
Combined total deferred inflows of resources	<u>330,597</u>	<u>177,091</u>	
Fund Balances:			
Restricted – Major Funds	4,370,220	4,156,376	
Restricted – Other Funds	96,978	85,253	
Assigned – Major Funds	2,146,097	1,891,750	
Unrestricted – Major Funds	(1,873,537)	(1,089,043)	
Combined total fund balances	<u>4,739,758</u>	<u>5,044,336</u>	
Total liabilities, deferred inflows of resources and fund balances	\$ 8,407,582	\$ 8,513,895	

Table 4			
Changes in Fund Balances	2013	2012	
Revenues:			
Total revenues – Major Funds	\$ 6,156,468	\$ 5,337,566	
Total revenues – Other Funds	546,904	845,795	
Combined total revenues	<u>6,703,372</u>	<u>6,183,361</u>	
Expenditures:			
Total expenditures – Major Funds	6,472,771	4,792,279	
Total expenditures – Other Funds	535,179	843,155	
Combined total expenditures	<u>7,007,950</u>	<u>5,635,434</u>	
Other financing sources (uses):			
Transfer – In	19,702	2,175	
Transfer – Out	(19,702)	(2,175)	
Combined other financing sources (uses), net	<u>-</u>	<u>-</u>	
Net changes in fund balance	(304,578)	547,927	
Fund Balance – beginning	5,044,336	4,496,409	
Fund Balance – ending	\$ 4,739,758	\$ 5,044,336	

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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, unassigned 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, 2013, the Municipality's governmental funds reported combined ending fund balances of \$4,739,758, a decrease of \$304,578 from the prior year.

The Municipality has an unassigned fund deficit of \$1,873,537 in its General Fund. The remainder balance of \$4,467,198 and \$2,146,097 is restricted and assigned, respectively.

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 2013 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, 2013 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.

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, 2013

LONG-TERM DEBT

At June 30, 2013 the Municipality had a total of \$5,132,531 in general obligations and other outstanding debts, as shown in **Table 6**. Of this amount, \$2,315,000 comprises debt backed by the full faith and credit of the government and \$2,817,531 is other obligations.

Table 6	
Long Term Debts	Amount
General obligations	\$ 2,315,000
Others	<u>2,817,531</u>
Total Long Term Debts	<u>\$ 5,132,531</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 POSITION
June 30, 2013**

	Governmental Activities
ASSETS:	
Cash	\$ 2,711,476
Cash with Fiscal Agent	2,141,703
Receivables (net):	
Property Tax	93,043
Sales Tax	8,316
Federal Grants	497,022
Intergovernmental	203,250
	5,654,810
Capital Assets:	
Property, Plant and Equipment	11,951,490
Accumulated Depreciation	(3,538,624)
Total Capital Assets	8,412,866
TOTAL ASSETS	14,067,676
 LIABILITIES:	
Accounts Payable and Accrued Expense	372,533
Bonds Payable	50,000
Accrued Interest	26,720
Due to Governmental Units	19,718
Unearned Revenue	115,484
Long-Term Liabilities:	
Due within One Year	182,405
Due in More than One Year	4,950,126
TOTAL LIABILITIES	5,716,986
DEFERRED INFLOWS OF RESOURCES	240,517
NET POSITION	
Invested in Capital Assets, Net of Related Debt	6,097,866
Restricted for:	
Debt Service	1,822,888
Other Purposes	2,644,310
Unrestricted (Deficit)	(2,454,891)
TOTAL NET POSITION	\$ 8,110,173

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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	\$ (587,048)	\$ -	\$ -	\$ -	\$ (587,048)
General Government	(2,518,994)	11,478	-	-	(2,507,516)
Public Safety	(159,369)	-	-	-	(159,369)
Public Works	(525,501)	-	-	-	(525,501)
Culture and Recreation	(204,354)	-	-	-	(204,354)
Sanitation	(711,241)	-	5,575	-	(705,666)
Human Services and Welfare	(441,645)	-	248,537	-	(193,108)
Urban Development	(1,536,980)	-	2,677	835,644	(698,659)
Education	(217,093)	-	161,413	-	(55,680)
Interest on Long-Term Debt	(54,575)	-	-	-	(54,575)
Total Governmental Activities	\$ (6,956,800)	\$ 11,478	\$ 418,202	\$ 835,644	(5,691,476)

General Revenues:

Taxes:

Property Taxes, levied for General Purposes	429,057
Property Taxes, levied for Debt Services	147,647
Volume of Business Taxes	157,136
Licenses and Permits	209,970
Sales Taxes, levied for Other Purposes	1,114,010
Sales Taxes, levied for Debt Services	276,060
Intergovernmental	2,898,220
Rent	15,375
Miscellaneous	266,672

Total General Revenues 5,514,147

CHANGE IN NET POSITION (177,329)

Net Position - Beginning of Year 8,287,502

NET POSITION - END OF YEAR \$ 8,110,173

See accompanying notes to basic financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

BALANCE SHEET - GOVERNMENTAL FUNDS
June 30, 2013

	General Fund	State Assignment Fund	Debt Service Fund	CDBG Fund	Other Governmental Funds	Total Funds
ASSETS						
Cash	\$ 2,152,378	\$ 376,899	\$ -	\$ 3,517	\$ 178,682	\$ 2,711,476
Cash with Fiscal Agent	-	45,652	1,895,125	-	200,926	2,141,703
Receivables:						
Property Tax	90,080	-	2,963	-	-	93,043
Sales Tax	6,796	-	1,520	-	-	8,316
Federal Grants	-	-	-	405,163	91,859	497,022
Intergovernmental	51,850	4,618	-	-	146,782	203,250
Due from Other Funds	496,160	2,202,394	-	-	54,218	2,752,772
TOTAL ASSETS	\$ 2,797,264	\$ 2,629,563	\$ 1,899,608	\$ 408,680	\$ 672,467	\$ 8,407,582
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCES						
Liabilities						
Accounts Payable and Accrued Liabilities	\$ 144,190	\$ 4,000	\$ -	\$ 224,343	\$ -	\$ 372,533
Bonds and Notes Payable	-	-	50,000	-	-	50,000
Accrued Interest	-	-	26,720	-	-	26,720
Due to Governmental Units	19,718	-	-	-	-	19,718
Due to Other Funds	2,155,232	78,231	-	184,337	334,972	2,752,772
Unearned Revenues:						
Volume of Business Tax	115,484	-	-	-	-	115,484
Total Liabilities	2,434,624	82,231	76,720	408,680	334,972	3,337,227
Deferred Inflows of Resources						
Unavailable Revenues:						
Property Taxes	90,080	-	-	-	-	90,080
Federal Grants	-	-	-	-	240,517	240,517
Total Deferred Inflows of Resources	90,080	-	-	-	240,517	330,597
Fund Balances						
Restricted	-	2,547,332	1,822,888	-	96,978	4,467,198
Assigned	2,146,097	-	-	-	-	2,146,097
Unassigned	(1,873,537)	-	-	-	-	(1,873,537)
Total Fund Balances	272,560	2,547,332	1,822,888	-	96,978	4,739,758
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCES	\$ 2,797,264	\$ 2,629,563	\$ 1,899,608	\$ 408,680	\$ 672,467	\$ 8,407,582

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, 2013

Total Fund Balances – Governmental Funds **\$ 4,739,758**

Amounts reported for Governmental Activities in the Statement of Net Position 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	90,080
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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	(2,315,000)	
Compensated Absences	(360,582)	
Law 42	(2,138,836)	
Law 146	(6,514)	
Health Insurance Administration	<u>(311,599)</u>	
Total Long-Term Liabilities		<u>(5,132,531)</u>

Total Net Position of Governmental Activities **\$ 8,110,173**

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, 2013

	General Fund	State Assignment Fund	Debt Service Fund	CDBG Fund	Other Governmental Funds	Total Funds
REVENUES						
Property Taxes	\$ 429,057	\$ -	\$ 147,647	\$ -	\$ -	\$ 576,704
Volume of Business Taxes	157,136	-	-	-	-	157,136
Sales Taxes	1,114,010	-	276,060	-	-	1,390,070
Federal Assistances	-	-	-	533,867	282,890	816,757
Intergovernmental	2,898,220	178,978	-	-	252,536	3,329,734
Licenses and Permits	209,970	-	-	-	-	209,970
Rent	15,375	-	-	-	-	15,375
Charges for Sales	-	-	-	-	11,478	11,478
Miscellaneous	190,573	5,575	-	-	-	196,148
Total Revenues	5,014,341	184,553	423,707	533,867	546,904	6,703,372
EXPENDITURES						
Current:						
Mayor and Municipal Legislature	587,048	-	-	-	-	587,048
General Government	2,520,144	-	-	-	-	2,520,144
Public Safety	159,369	-	-	-	-	159,369
Public Works	525,501	-	-	-	-	525,501
Culture and Recreation	204,354	-	-	-	-	204,354
Sanitation	711,241	-	-	-	-	711,241
Human Services and Welfare	186,352	-	-	-	255,293	441,645
Urban Development	572,445	289,841	-	553,569	121,125	1,536,980
Education	58,332	-	-	-	158,761	217,093
Debt Service:						
Principal	-	-	50,000	-	-	50,000
Interest and Other Charges	-	-	54,575	-	-	54,575
Total Expenditures	5,524,786	289,841	104,575	553,569	535,179	7,007,950
Excess (deficiency) of revenues over (under) expenditures	(510,445)	(105,288)	319,132	(19,702)	11,725	(304,578)
OTHER FINANCING SOURCES (USES)						
Transfer- In	-	-	-	19,702	-	19,702
Transfer- Out	(19,702)	-	-	-	-	(19,702)
Total Other Financing Sources and Uses	(19,702)	-	-	19,702	-	-
Net Change in Fund Balances	(530,147)	(105,288)	319,132	-	11,725	(304,578)
Fund Balance - Beginning as Restated	802,707	2,652,620	1,503,756	-	85,253	5,044,336
FUND BALANCES - ENDING	\$ 272,560	\$ 2,547,332	\$ 1,822,888	\$ -	\$ 96,978	\$ 4,739,758

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, 2013

Net Change in Fund Balances – Total Governmental Funds	\$ (304,578)
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	90,080
Revenues in the governmental funds that correspond to prior year resources are not recorded as revenue in the Statement of Activities	(13,981)
Repayment of debt proceeds principal is expenditure in the governmental funds, but the repayment reduces Long-Term Liabilities in the Statement of Net Position. In the current year the repayments were	50,000
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	37,760
Decrease in Law 42	57,923
Increase in Health Insurance Administration	(94,876)
Decrease in Law 146	<u>343</u>
Total Additional Expenditures	<u>1,150</u>
Change in Net Position of Governmental Activities	<u>\$ (177,329)</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, 2013**

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 five 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, 2013, 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, 2013, 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, 2013**

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, 2013, 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, 2013**

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 Positions 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 assets by the provider and a liability 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, 2013, 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, 2013

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 Position 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 Position 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 Position** – These results when constraints are placed on net position 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 Position** – These consists of net position which do not meet the definition of the two preceding categories. Unrestricted net position often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net position 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 position or liabilities changed during the fiscal year ended June 30, 2013, 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, 2013

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, 2013

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, 2013

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 positions 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, 2013

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, 2013

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:

- ❖ **Non-spendable** – 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 non-spendable, 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, 2013.

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, 2013, the accompanying fund financial statements reported fund balances as restricted and unassigned.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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, 2013**

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.

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, 2013, 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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

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

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

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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

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, 2013.

<u>BALANCE JULY 1, 2012</u>	<u>NEW ISSUES</u>	<u>RETIREMENTS AND CURRENT MATURATES</u>	<u>BALANCE JUNE 30, 2013</u>	<u>CURRENT PORTION</u>	<u>LONG-TERM PORTION</u>
\$ 398,342	\$ _____	\$ 37,760	\$ 360,582	\$ 65,500	\$ 295,082

M. 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 sent to the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

N. Inter-fund 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:

- ❖ **Inter-fund 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.
- ❖ **Inter-fund 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.
- ❖ **Inter-fund reimbursements** – Represent repayments from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

O. 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.

P. 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.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Q. 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.

R. 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, 2013 amounted to \$102,433. The current insurance policies have not been cancelled or terminated. The CRIM also deducted \$105,372 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, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

S. Future Adoption of Accounting Pronouncements

The GASB has issued the following accounting standards that have effective dates after June 30, 2013:

- ❖ 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.
- ❖ GASB Statement No. 70 *Accounting and Financial Reporting for Non-exchange Financial Guarantees*. This statement is effective for periods beginning after June 15, 2013.
- ❖ GASB Statement No. 71 *Pension Transition for Contributions made Subsequent to the Measurement Date- an amendment of GASB 68*. This statement is effective for periods beginning after June 15, 2014.

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.

NEW ACCOUNTING STANDARDS

The provisions of the following Governmental Accounting Standards Board (GASB) Statement have been implemented for the year ended June 30, 2013:

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources.

GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement established accounting and financial reporting that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as revenues and expenses

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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, 2013.

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, 2013, (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, 2013, 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, 2013, 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, 2013. Therefore, the Municipality's management has concluded that at June 30, 2013 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, 2013.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

The Municipality's bank balances in commercial banks of \$2,152,378 in the General Fund, \$376,899 in the State Assignment Fund and \$3,517 in the CDBG Fund were fully collateralized at June 30, 2013. Also, in the Other Governmental Funds there were deposits with commercial banks of \$178,682 that were fully collateralized.

The deposits at GDB of \$45,652 in the State Assignment Fund, \$1,895,125 in the Debt Service Fund and \$200,926 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	\$ 405,163
Child Care Development Block Grant	70,330
Special Programs for the Aging Title III-Part B	<u>21,529</u>
Total	<u>\$ 497,022</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>
Office of the Commissioner of Municipal Affairs	\$ 51,850
State Port Authority	4,618
State Department of Labor – Law 52	<u>146,782</u>
Total	<u>\$ 203,250</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

NOTE 3 – RECEIVABLES (CONTINUED)

C. Due From Other Funds

Interfund receivables and payables at June 30, 2013 are summarized as follows:

Receivable Fund	Payable Fund	Purpose	Amount
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed	\$ 236,849
General Fund	State Assignment Fund	Payroll and related accruals paid and not reimbursed	78,231
General Fund	CDBG Fund	Payroll and related accruals paid and not reimbursed	181,080
State Assignment Fund	General Fund	Loans between funds	2,101,014
State Assignment Fund	Other Governmental Funds	Loans between funds	98,123
State Assignment Fund	CDBG	Loans between funds	3,257
Other Governmental Funds	General Fund	Cash pool in the same bank account	<u>54,218</u>
Total			<u>\$ 2,752,772</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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 2013, including those changes pursuant to the implementation of GASB Statement No. 34, follows (Land and construction in progress are not subject to depreciation):

Governmental Activities	Balance July 1, 2012	Additions	Retirements / Reclassifications	Balance June 1, 2013
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>-</u>	<u>-</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>-</u>	<u>-</u>	<u>1,626,395</u>
Total capital assets being depreciated	<u>8,584,604</u>	<u>-</u>	<u>-</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>-</u>	<u>-</u>	<u>(1,428,602)</u>
Total accumulated depreciation	<u>(3,538,624)</u>	<u>-</u>	<u>-</u>	<u>(3,538,624)</u>
Total capital assets being depreciated, net	<u>5,045,980</u>	<u>-</u>	<u>-</u>	<u>5,045,980</u>
Governmental activities capital assets, net	<u>\$ 8,412,866</u>	<u>\$ -</u>	<u>\$ -</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>

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 complied with GASB Statement No. 34.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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 2012-2013, and not paid by the Municipality at June 30, 2013. Following is a detail of these accounts payable and accrued liabilities:

Major Governmental Funds	Accounts Payable	Accrued Liabilities	Total
General Fund	\$ 59,861	\$ 84,329	\$ 144,190
State Assignment Fund	4,000	-	4,000
CDBG Fund	<u>224,343</u>	<u>-</u>	<u>224,343</u>
Total	<u>\$ 288,204</u>	<u>\$ 84,329</u>	<u>\$ 372,533</u>

NOTE 6 – DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2013, balance due to other governmental units consists of the following:

Governmental Agency	Amount
General Service Administration	\$ 3,887
Aqueduct and Sewer Authority	2,861
State Department of Labor	10,016
State Insurance Fund Corporation	<u>2,954</u>
Total	<u>\$ 19,718</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

NOTE 7 – DEFERRED INFLOWS OF RESOURCES

- A. Property Taxes** – the deferred inflows of resources of \$90,080 in the General Fund are the property taxes that represents advances from fiscal year 2012-2013, not collected by the Municipality at June 30, 2013.
- B. Federal Grants** – the deferred inflows of resources presented in Other Governmental Funds represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred inflows of resources from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Child Care Food Program	\$ 46,686
Public Assistance Grants	169,601
Child Care Development Block Grant- ARRA	77
Homelessness Prevention and Rapid Re-housing Program- ARRA	53
Energy Efficiency and Conservation Block Grant- ARRA	<u>24,100</u>
Total	<u>\$ 240,517</u>

NOTE 8 – GENERAL LONG-TERM DEBTS

Long-term liability activity for the year ended June 30, 2013, 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	\$ 2,365,000	\$ -	\$ 50,000	\$ 2,315,000	\$ 55,000
Property Tax Debt – Law 42	2,196,759	-	57,923	2,138,836	61,562
Compensated absences	398,342	-	37,760	360,582	65,500
Property Tax Debt – Law 146	6,857	-	343	6,514	343
Health Insurance Administration	<u>216,723</u>	<u>94,876</u>	<u>-</u>	<u>311,599</u>	<u>-</u>
Total	<u>\$ 5,183,681</u>	<u>\$ 94,876</u>	<u>\$ 146,026</u>	<u>\$ 5,132,531</u>	<u>\$ 182,405</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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, 2013, 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	\$ 1,945,000
\$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>370,000</u>
Total General Obligations – Bonds	<u>\$ 2,315,000</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, 2013 are as follows:

Year Ending June 30,	Principal payment	Interest payment	Total
2014	\$ 55,000	\$ 127,200	\$ 182,200
2015	60,000	169,500	229,500
2016	60,000	165,000	225,000
2017	70,000	160,500	230,500
2018	75,000	155,251	230,251
2019-2023	460,000	684,005	1,144,005
2024-2028	660,000	484,504	1,144,504
2029-2033	<u>875,000</u>	<u>197,254</u>	<u>1,072,254</u>
Total	<u>\$ 2,315,000</u>	<u>\$ 2,143,214</u>	<u>\$ 4,458,214</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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, 2013 amounted to \$2,138,836.

D. COMPENSATED ABSENCES

The government-wide statement of net position includes \$360,582 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, 2013 amounted to \$6,514.

F. HEALTH INSURANCE ADMINISTRATION

Liabilities of \$311,599 reported in the statement of net position represent the balance owed for services provided by the State Insurance Health Administration to the Municipality and not paid at June 30, 2013.

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 position date. The accompanying statement of net position 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, 2013.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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, 2013 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, 2013 was 8.83% (of which 7.77% 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, 2013**

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, 2013, 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 unearned revenues in the GWFS and the GFFS.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

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 10th 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, 2013**

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 defined 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 be 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, 2013**

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, 2013 was approximately \$94,970. 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, 2013. 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, Puerto Rico 00940.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

NOTE 15 – CONTINGENCIES

A. CLAIMS AND JUDGMENTS

The Municipality is, at present, a defendant in a number of legal claims and proceedings that arise from alleged improper application of policies and negligence in the ordinary course of the Municipality's activities. The claims and legal judgments amounts to approximately \$2 million.

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, 2013 of approximately \$125,000 for the construction, improvements, or renovation of several capital facilities and the capital assets.

D. OTHER COMMITMENTS

At June 30, 2013 the General Fund had commitments of approximately \$149,993 for executory purchase orders or contracts that will be honored during the subsequent year.

NOTE 16 – FUND BALANCE (DEFICIT)

As of June 30, 2013, the fund balance (deficit) classifications are as follows:

Fund Balance (Deficit)	General Fund	State Assignment Fund	Debt Service Fund	Other Governmental Fund	Total
Restricted for:					
Human Services and Welfare	\$ -	\$ -	\$ -	\$ 90	\$ 90
Urban Development	-	2,547,332	-	38,370	2,585,702
Education	-	-	-	58,518	58,518
Debt Service	-	-	1,822,888	-	1,822,888
Total restricted	<u>-</u>	<u>2,547,332</u>	<u>1,822,888</u>	<u>96,978</u>	<u>4,467,198</u>
Assigned for:					
Urban Development	2,146,097	-	-	-	2,146,097
Unassigned	<u>(1,873,537)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,873,537)</u>
Total Fund Balance (Deficit)	<u>\$ 272,560</u>	<u>\$ 2,547,332</u>	<u>\$ 1,822,888</u>	<u>\$ 96,978</u>	<u>\$ 4,739,758</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

NOTES TO THE BASIC FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

NOTE 17 – SUBSEQUENT EVENTS

On April 4, 2013 the Legislature of the Commonwealth of Puerto Rico issued Act. No. 3, which amends the previously issued Act 447 of 1951 ("Retirement System Act"). This Act make significant changes to the Employees Retirement System of the Commonwealth of Puerto Rico trust created by Act 447 of May 15, 1951, as amended, to provide pension and other benefits to retired employees of the government of Puerto Rico and its instrumentalities. The changes established in Act No. 3 will apply to all employees participating in the Retirement System for the period starting in July 1, 2013.

Management has evaluated subsequent events through February 28, 2014, 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, 2014.

**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, 2013

	<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	\$ 429,057	\$ 429,057	\$ 429,057	\$ -
Volume of Business Taxes	213,176	213,176	157,136	(56,040)
Intergovernmental Revenues	2,758,820	2,758,820	2,898,220	139,400
Licenses, permits and other local taxes	644,840	644,840	209,970	(434,870)
Rent of Property	36,000	36,000	15,375	(20,625)
Miscellaneous	<u>1,162,398</u>	<u>1,162,398</u>	<u>190,573</u>	<u>(971,825)</u>
Total revenues	<u>5,244,291</u>	<u>5,244,291</u>	<u>3,900,331</u>	<u>(1,343,960)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
Mayor and Municipal Legislature	711,254	747,054	636,215	110,839
General government	2,519,961	2,469,261	2,222,987	246,274
Public safety	242,196	239,196	160,767	78,429
Public works	625,211	617,211	532,452	84,759
Culture and Recreation	230,462	238,862	205,389	33,473
Sanitation	632,617	662,117	622,802	39,315
Human Service and Welfare	198,718	198,718	186,447	12,271
Human Service and Welfare	<u>83,872</u>	<u>71,872</u>	<u>58,332</u>	<u>13,540</u>
Total expenditures, encumbrances and other financing uses	<u>5,244,291</u>	<u>5,244,291</u>	<u>4,625,391</u>	<u>618,900</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (725,060)</u>	<u>\$ (725,060)</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTE TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2013**

**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	\$ 3,900,331
Differences-budget to GAAP:	
Prior and current GAAP adjustments to revenues	<u>1,114,010</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$ 5,014,341</u>

Uses/outflows of resources:

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	\$ 4,625,391
Differences-budget to GAAP:	
Prior Year expenditure are not outflows of budgetary resources but are expenditure for financial purposes	224,443
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(149,993)
GAAP adjustment to expenditures	<u>824,945</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$ 5,524,786</u>



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

Certified Public Accountants and Financial Consultants

**INDEPENDENT AUDITOR'S 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,
Members of the Municipal Legislature
and People of the Municipality of Culebra
Culebra, Puerto Rico

We have audited, in accordance with the 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, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Culebra of the Commonwealth of Puerto Rico (the Municipality), as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated February 28, 2014. We did not express an opinion on the governmental-wide financial statements because we were unable to obtain sufficient and competent evidential matter related to capital assets and estimated landfill closure and post-closure care cost liability.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Municipality's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of Municipality's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

**INDEPENDENT AUDITOR'S 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)

Internal Control Over Financial Reporting (Continued)

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 2013-II-1 and 2013-II-2 to 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. The results of our tests did not disclose any significant deficiency that are required to be reported under Government Auditing Standards.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free from 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 did not disclose any instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Municipality's Response to Findings

Municipality's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Municipality's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

INDEPENDENT AUDITOR'S 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)

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Nieves Velazquez & Co., P.S.C.
NIEVES VELAZQUEZ & CO., P.S.C.

San Juan, Puerto Rico
February 28, 2014

CPA Stamp No. 02696603 was affixed
to the original of this report.





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

Certified Public Accountants and Financial Consultants

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133**

To the Honorable Mayor,
Members of the Municipal Legislature
and People of the Municipality of Culebra
Culebra, Puerto Rico

Report on Compliance for Each Major Federal Program

We have audited the Municipality of Culebra of the Commonwealth of Puerto Rico (the Municipality) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have direct and material effect on each of the Municipality of Culebra of the Commonwealth of Puerto Rico major federal programs for the year ended June 30, 2013. The Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Municipality's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Municipality's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133
(Continue)**

Auditor's Responsibility (Continued)

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Municipality's compliance.

Basis for Qualified Opinion on CDBG Major Federal Program

As described in the accompanying schedule of findings and questioned costs, the Municipality's did not comply with requirements regarding CFDA 14-228, Community Development Block Grant (CDBG) as described in findings numbers 2013-III-5 for period of availability of federal funds, 2013-III-1 for equipment and real property management, 2013-III-3 for cash management and 2013-III-4 for reporting. Compliance with such requirements is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

Qualified Opinion on CDBG Major Federal Program

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the Municipality, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the Community Development Block Grant for the year ended June 30, 2013.

Other Matters

The results of our auditing procedures disclosed other instances of noncompliance, 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 2013-III-2. Our opinion on each major federal program is not modified with respect to these matters.

The Municipality's response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133
(Continue)**

Report on Internal Control Over Compliance

Management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Municipality's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program 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 the Municipality'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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and 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 item 2013-III-5 to be a material weakness.

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 2013-III-1, 2013-III-3 and 2013-III-4 to be significant deficiencies.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE
FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133
(Continue)**

Report on Internal Control Over Compliance (Continued)

The Municipality's response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

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

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

San Juan, Puerto Rico

February 28, 2014

CPA Stamp No. 02696604 was affixed
to the original of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2013**

<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>			
Pass-Through the Commonwealth of Puerto Rico – Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	\$ 22,635
Total U.S. Department of Agriculture			<u>22,635</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	553,569
Total Community Development Block Grants – Cluster			<u>553,569</u>
Pass-Through State – State Department of Family:			
Homelessness Prevention and Rapid Re-Housing Program (Recovery Act Funded)	14.257	Not Available	<u>500</u>
Total U.S. Department of Housing and Urban Development			<u>554,069</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>1,905</u>
Pass-Through State - Administration for Children and Families:			
Child Care and Development Block Grant	93.575	Not Available	<u>135,051</u>
Total U.S. Department of Health and Human Service			<u>136,956</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$713,660</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2013**

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.

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, 2013**

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><i>Fund</i></u>	<u><i>Federal Assistance</i></u>	<u><i>Other Assistance</i></u>	<u><i>Financial Statements</i></u>
<i>CDBG Fund</i>	\$553,569	-	553,569
Other Governmental Funds	<u>160,091</u>	<u>375,088</u>	<u>535,179</u>
Totals	<u>\$713,660</u>	<u>375,088</u>	<u>1,088,748</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013**

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 | Unmodified | |
| | ❖ Material weakness (es) identified? | <u> x </u> Yes | ___ No |
| | ❖ Significant deficiency (ies) identified? | ___ Yes | <u> x </u> No |
| 3. | Noncompliance material to financial statement noted? | ___ Yes | <u> x </u> No |

Part II. Federal Awards

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

4. Identification of major programs:

<u>Name of Federal Program or Cluster</u>	<u>CFDA Number (s)</u>
Community Development Block Grant	14.228

- | | | |
|----|---|-----------------------|
| 5. | Dollar threshold used to distinguish between Type A and Type B programs | \$300,000 |
| 6. | Auditee qualified as low-risk auditee? | ___ Yes <u> x </u> No |

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013**

Section II. Financial Statement Findings

FINDING	13-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 in a separate letter.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013

Section II. Financial Statement Findings

FINDING	13-II-2
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 in a separate letter.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013**

Section III – Federal Award Findings and Questioned Costs

FINDING	13-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 complete property register that includes all the required information; it only includes the property number in some of them and its description. A physical inventory was taken in April 2013 however, it has not been reconciled with the accounting records.
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.
QUESTIONED COSTS	NONE
MANAGEMENT RESPONSE	See Corrective Action Plan in a separate letter.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013**

Section III – Federal Award Findings and Questioned Costs

FINDING	13-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, 2013

Section III – Federal Award Findings and Questioned Costs

FINDING	13-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 in a separate letter.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013**

Section III – Federal Award Findings and Questioned Costs

FINDING	13-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. As per contract agreement, the program cannot maintain the cash in bank for no more than three (3) business days. After deposits examined, we noted that the program held excess of cash on bank account between 6 and 33 business days. We conclude that the program does not comply with this audit requirement during the audited year ended on June 30, 2013. This finding is repeated from prior years.
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).
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 in a separate letter.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013**

Section III – Federal Award Findings and Questioned Costs

FINDING 13-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 all quarterly reports were not filed on time. The details of the submitted reports is a follows:

#	Program Year	Report Period Covered		Date Submitted	Limited Date	Submitted On Time?
		From	To			
1	2013	7/1/2012	9/30/2012	11/14/2012	10/15/2012	No
2	2013	10/1/2012	12/31/2012	3/19/2013	1/15/2013	No
3	2013	1/1/2013	3/31/2013	5/1/2013	4/15/2013	No
4	2013	4/1/2013	6/30/2013	7/29/2013	7/15/2014	No

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 Lack of adequate supervision to submit the reports on time.

EFFECT The late submissions of such reports may cause an improper hand ling of amounts been expensed and obligated.

RECOMMENDATION The Program Director should request, to the employees, by written form to provide the reports on the required time.

QUESTIONED COSTS NONE

MANAGEMENT RESPONSE See Corrective Action Plan in a separate letter.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2013

Section III – Federal Award Findings and Questioned Costs

FINDING	13-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 2009 and 2010 and amounting to \$690,379 and \$858,891, respectively, 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 in a separate letter.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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>
06/30/2012	CDBG	12-11-1	<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>	<p>Finding repeated in the current year. (13-II-1)</p>
06/30/2012	CDBG	12-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 a 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>	<p>The Municipality hires every year an external consultant to prepare the financial statements from the availability accounting computerized and manual systems. Also, the Municipality is considering to acquire a new accounting software system.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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>
06/30/2012	CDBG	12-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>	
06/30/2012	CDBG	12-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 13-II-2)
06/30/2012	CDBG	12-II-4	<p>Supporting Payment Documents</p> <p>Criteria and Condition:</p> <p>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.</p> <p>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.</p>	Supporting payment documents were not located during the year 06/30/2013.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA**

**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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>
06/30/2012	CDBG	12-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. (13-III-1)
06/30/2012	CDBG	12-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". 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> <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. (13-III-2)

**COMMONWEALTH OF PUERTO RICO
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**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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>
06/30/2012	CDBG	12-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 Affair).</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. (13-III-3)
06/30/2012	CDBG	12-III-4	<p>Reporting</p> <p>Criteria and Condition:</p> <p>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.</p> <p>During our Test of Reporting we found one quarterly report (04/12-06/30/12) filed 26 days after the due date and for the other three quarterly report no submission evidence was provided.</p>	Finding repeated in the current year. (13-III-4)

**COMMONWEALTH OF PUERTO RICO
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**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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>
06/30/2012	CDBG	12-III-5	<p>Period of Availability of Federal Funds</p> <p>Criteria and Condition:</p> <p>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 15 months and the period to expense is 4 years.</p> <p>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.</p>	Finding repeated in the current year (13-III-5).
06/30/2011	CDBG	11-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 properly 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. (13-II-1)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF CULEBRA

PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013

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	11-II-2	Accounting System	
			Criteria and Condition:	
			According to Article 8.010(a) and (b) of Law No. 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.	Finding not repeated in the current year.
			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.	

**COMMONWEALTH OF PUERTO RICO
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**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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	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>	<p>Finding repeated in the current year. (See 13-II-2)</p>
06/30/2011	CDBG	11-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>	<p>Finding repeated in the current year. (See 13-III-1)</p>

**COMMONWEALTH OF PUERTO RICO
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**PRIOR YEARS FINDINGS AND QUESTIONED COSTS
Year ended June 30, 2013**

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	11-III-2	<p>Lack 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 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 sub-awards are not suspended or debarred from participation if federal programs.</p>	Finding repeated in the current year. (See 13-III-2)
06/30/2011	CDBG	11-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 to the Pass-through State - Office of Commissioner of Municipal Affair. We noted disbursements elapsing between 10 to 68 days. This finding is repeated from prior years.</p>	Finding repeated in the current year. (See13-III-1)



CORRECTIVE ACTION PLAN
SINGLE AUDIT 2012-2013

Financial Statements Findings

Finding 13-II-1- Equipment and Real Property Management

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 Garcia Martínez



13-II-2- 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

Federal Award Findings

13-III-1- Equipment and Real Property Management

Federal Program Department does not have a complete property register that includes all the required information; it only includes the property number in some of them and its description. A physical inventory was taken in April 2013 however, it has not been reconciled with the accounting records.



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

13-III-2- Suspension and Debarment

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

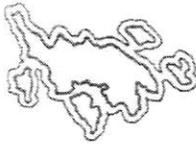
In testing procurement, suspension and debarments, we were not able to find evidence indicating that the Municipality performs procedures to assure that the individuals and entities that receive contracts or sub-awards are not suspended or debarred from participation in federal programs. For example, we found an instance where municipality official could not provide the contract file that 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.

Responsible Person

Brenda Cruz Walker



13-III-3- Cash Management

The program does not maintain proper procedures to minimize time elapsing between funds received and disbursed. As per contract agreement the program cannot maintain the cash in bank for more than three (3) business days. After deposits examined, we noted that the program held excess of cash on bank account between 6 to 33 business days. We concluded that the program does not comply with this audit requirement during the audited year ended on June 30, 2013. This finding is repeated from prior years.

Corrective Action

The finance department and the federal department together establish a process where once the funds are received; the finance department notifies the federal department to proceed immediately with the order of disbursement. As soon as the Department of Finance receives from the department of federal the disbursement order, will proceed with the payment of such order. This must occur within 3 days established for that disbursement of funds.

Responsible Person

Brenda Cruz Walker
Frank García Martínez

13-III-4- Reporting

During our Test of Reporting we found all quarterly reports were not filed on time.

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.

The quarterly reports for the months of January 2013 to March 2013 and April 2013 to June 2013 were submitted on time to the pass-through entity.

Responsible Person

Brenda Cruz Walker



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

During our Test of Availability of Federal Funds we noted that funds pertaining to year 2009 and 2010 and amounting to \$690,379 and \$858,891 respectively were not obligated within the 24 months period required.

Corrective Action

Processes will be established to ensure that existing funds are obliged within the period of 24 months established.

Responsible Person

Brenda Cruz Walker

Responsible Officials.


William I. Solis Bermúdez
Mayor


Frank García Martínez
Finance Department Director


Brenda Cruz Walker
Federal Program Director