

09 JUN 15 PM 12:09
UNIDAD DE CORREO

Cap/201/1259

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
BASIC FINANCIAL STATEMENTS

FISCAL YEAR ENDED JUNE 30, 2008

(WITH THE ADDITIONAL REPORTS AND INFORMATION REQUIRED BY
THE GOVERNMENT AUDITING STANDARDS AND OMB CIRCULAR A-133)

27

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
BASIC FINANCIAL STATEMENTS
FISCAL YEAR ENDED JUNE 30, 2008
(WITH THE ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE GOVERNMENT AUDITING STANDARDS
AND OMB CIRCULAR A-133)**

TABLE OF CONTENTS

	Pages
PART I – Financial:	
Independent Auditors' Report	2- 3
Management's Discussion and Analysis	4-17
Basic Financial Statements:	
Governmental-Wide Statements:	
Statement of Net Assets	18
Statement of Activities	19
Governmental Funds Statements:	
Balance Sheet	20-21
Statement of Revenues, Expenditures and Changes in Fund Balances	22-23
Notes to the Basic Financial Statements	24-36
Required Supplementary Information:	
Budgetary Comparison Schedule – General Funds	37
Note to Required Supplementary Information	38
PART II – Schedule of Expenditures of Federal Awards and Reports Required by Government Auditing Standards and OMB Circular A-133:	
Schedule of Expenditures of Federal Awards	40
Notes to Schedule of Expenditures of Federal Awards	41
Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	42-43
Independent Auditors' Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133	44-45
PART III – Findings and Questioned Costs:	
Schedule of Findings and Questioned Costs	47-49
Schedule of Prior Audits' Findings and Questioned Costs	50

PART I
FINANCIAL



201 Gautier Benítez Ave.
Consolidated Mall C-31
PO Box 8369
Caguas, PR 00726-8369
Phones: (787) 746-0510 / 746-1185 / 746-1370
Fax: (787) 746-0525
cpadiazmartinez@hotmail.com

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Member of the Municipal Legislature
Municipality of Fajardo, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Fajardo, Puerto Rico (Municipality)**, as of and for the fiscal year ended June 30, 2008, which collectively comprise the **Municipality's** basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the **Municipality's** management. Our responsibility is to express an opinion on these basic combined 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 basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statements presentation. We believe that our audit provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality**, as of June 30, 2008, and the respective changes in financial position, for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 18, 2008 on our consideration of the **Municipality's** internal control over financial reporting on our test of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis and budgetary comparison information on pages 4 through 17 and 37 and 38, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



INDEPENDENT AUDITORS' REPORT

Page 2

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

CPA Diaz-Martinez, PSC

CPA DIAZ-MARTINEZ, PSC
Certified Public Accountants & Consultants
License Number 12, expires on December 1, 2010

Caguas, Puerto Rico
December 18, 2008



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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

The following discussion and analysis of the Municipality of Fajardo' financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2008. Please read it in conjunction with the financial statements which follow this section.

FINANCIAL HIGHLIGHTS

Highlights for Government-wide Financial Statements

The government-wide financial statements report information about the Municipality as a whole using the economic resources measurement focus and accrual basis of accounting:

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2008 by \$113,364,973 (net assets).
- Revenues increased by \$728,489 and expenses decreased by \$391,374, in comparison with year 2007, as restated.
- Net change in net assets amounted to \$7,688,233
- An increase of 7% with respect to prior year (2008) net change.

Highlights for Fund Financial Statements

The fund financial statements provide detailed information about the Municipality's most significant funds using the current financial resources measurement focus and modified accrual basis of accounting:

- At the close of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$51,298,824, an increase of \$2,250,340 in comparison with the prior year.
- The General Fund reported an excess of expenditures over revenues and other financing uses of \$5,467,392 and an unreserved fund balance of \$7,116,330. Unreserved fund balances increased by \$2,962,593 from prior year.

General Financial Highlights

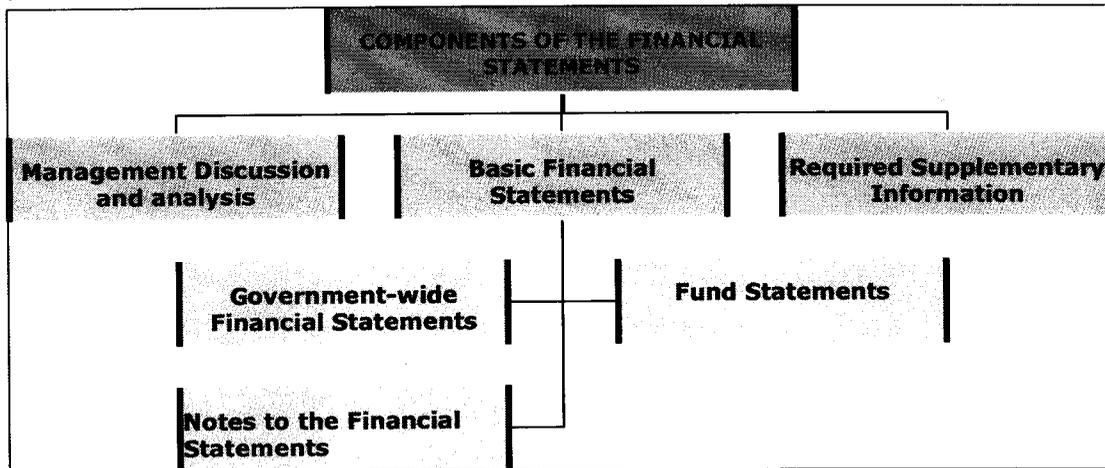
- The investment in net capital assets as of June 30, 2008 was \$75,688,196 (net of related debt).
- Long-term debt general and special obligations decreased by \$723,000 approximately 4% with respect to prior year balance.
- Other long-term debts decreases and net reductions from payments amounted to \$404,612 respectively.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$8,210,301.
- We underestimated the Licenses and Permits revenues by \$853,873, although we made economies on all expenditures.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

OVERVIEW OF THE FINANCIAL STATEMENTS

The Municipality's basic financial statements comprise three components: (1) management discussion and analysis (presented here), (2) basic financial statements, and (3) required supplementary information.



The Municipality's basic financial statements consist of two kinds of statements, each with a different view of the Municipality's finances. The government-wide financial statements provide both long-term and short-term information about the Municipality's overall financial status. The fund financial statements focus on major aspects of the Municipality's operations, reporting those operations in more detail than the government-wide statements:

Basic Financial Statements

- ***Government-Wide Financial Statements***

The government-wide statements report information about the Municipality as a whole using accounting methods similar to those used by private-sector businesses. They are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The first government-wide statement – the *Statement of Net Assets* – presents information on all of the Municipality's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in the Municipality's net assets are an indicator of whether its financial health is improving or deteriorating. Other non-financial factors such as the condition of the Municipality's roads and other infrastructure may need to be considered to assess the overall health of the Municipality. The second statement – the *Statement of Activities* – presents information showing how the net assets changed during the year. All of the current year's revenues and expenses are taken into account in the statement of activities regardless of when cash is received or paid.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

The government-wide statements reports as governmental activities the Municipality's basic services such as public safety, public works, health and sanitation, culture and recreation, solid waste disposal, human services and welfare, and community development; education and general administration. These activities are primarily financed through property taxes, other local taxes and intergovernmental revenues. Included in the governmental activities are the governmental funds.

- ***Fund Financial Statements***

The fund financial statements provide more detailed information about the Municipality's most significant funds. Funds are accounting devices that the Municipality uses to keep track of specific sources of funding and spending for particular purposes. Some funds are required by Federal and Commonwealth regulations, as well by bond covenants.

The Municipality's basic services are included in governmental funds, which are used to account for essentially the same functions reported as governmental activities in the government-wide statements. However, unlike the government-wide statements, the governmental funds are prepared using the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under this approach the financial statements focus on near-term inflows and outflows of external resources, as well on balances of expendable resources available at year end. Consequently, the governmental fund statements provide a detailed short-term view that helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, additional information is provided on a subsequent page that explains the relationship (or differences) between the government-wide and fund statements.

The governmental fund statements focus on major funds. The Municipality's major funds are the general fund (which accounts for the main operating activities of the Municipality) and funds that complies with a minimum criterion (percentage of the assets, liabilities, revenues or expenditures). Funds that do not comply with this criterion are grouped and presented in a single column as other governmental funds.

- ***Notes to the financial statements***

Provides integral information needed to explain the basis for the numbers used within the Basic Financial Statements and provide more detailed data.

Required supplementary information

Provides additional information to better understand the financial position of the Municipality and contains the Budgetary Comparison Schedule for the General Fund.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

The following table presents a summary of the Statements of Net Assets as of June 30, 2008 and 2007:

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. Net assets for the year increased 7.0% with respect to prior year as restated. The most significant changes were an increase in restricted assets of \$7,688,233.

Table 1		
Commonwealth of Puerto Rico Municipality of Fajardo, Puerto Rico Statement of Net Assets As of June 30, 2008		
	2008	2007
Current and non-current assets.....	\$ 62,271,482	\$ 59,580,926
Capital assets.....	<u>83,875,758</u>	<u>80,128,030</u>
Total Assets	<u>146,147,240</u>	<u>139,708,956</u>
Current liabilities.....	1,321,527	1,417,109
Deferred revenues.....	4,740,629	4,767,384
Long-term liabilities.....	<u>26,720,111</u>	<u>27,847,723</u>
Total Liabilities	<u>32,782,267</u>	<u>34,032,216</u>
Net Assets:		
Investment in capital assets, Net of Related Debt.....	75,688,196	57,722,330
Restricted.....	27,292,355	8,332,956
Unrestricted.....	<u>10,384,422</u>	<u>3,298,964</u>
Total Net Assets	<u>\$113,364,973</u>	<u>\$105,676,740</u>

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure) for \$75,688,233; total capital assets (\$83,875,758) net of accumulated depreciation and less any related outstanding debt (\$8,187,562) used to acquire or construct those assets. The Municipality uses these assets to provide services to its citizens and consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other

sources, because capital assets are not generally liquidated for the purposes of retiring debt.

Restricted net assets represent resources that are subject to external restrictions on how they may be used.

Unrestricted net assets are the part of the net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements.

As of June 30, 2008, the Municipality presented unrestricted net assets of \$10,384,422. This balance was affected by long-term obligations such as compensated absences \$3,360,369 and other debts in the amount of \$1,034,742 for which the Municipality did not provide funding in previous budgets. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Changes in net assets

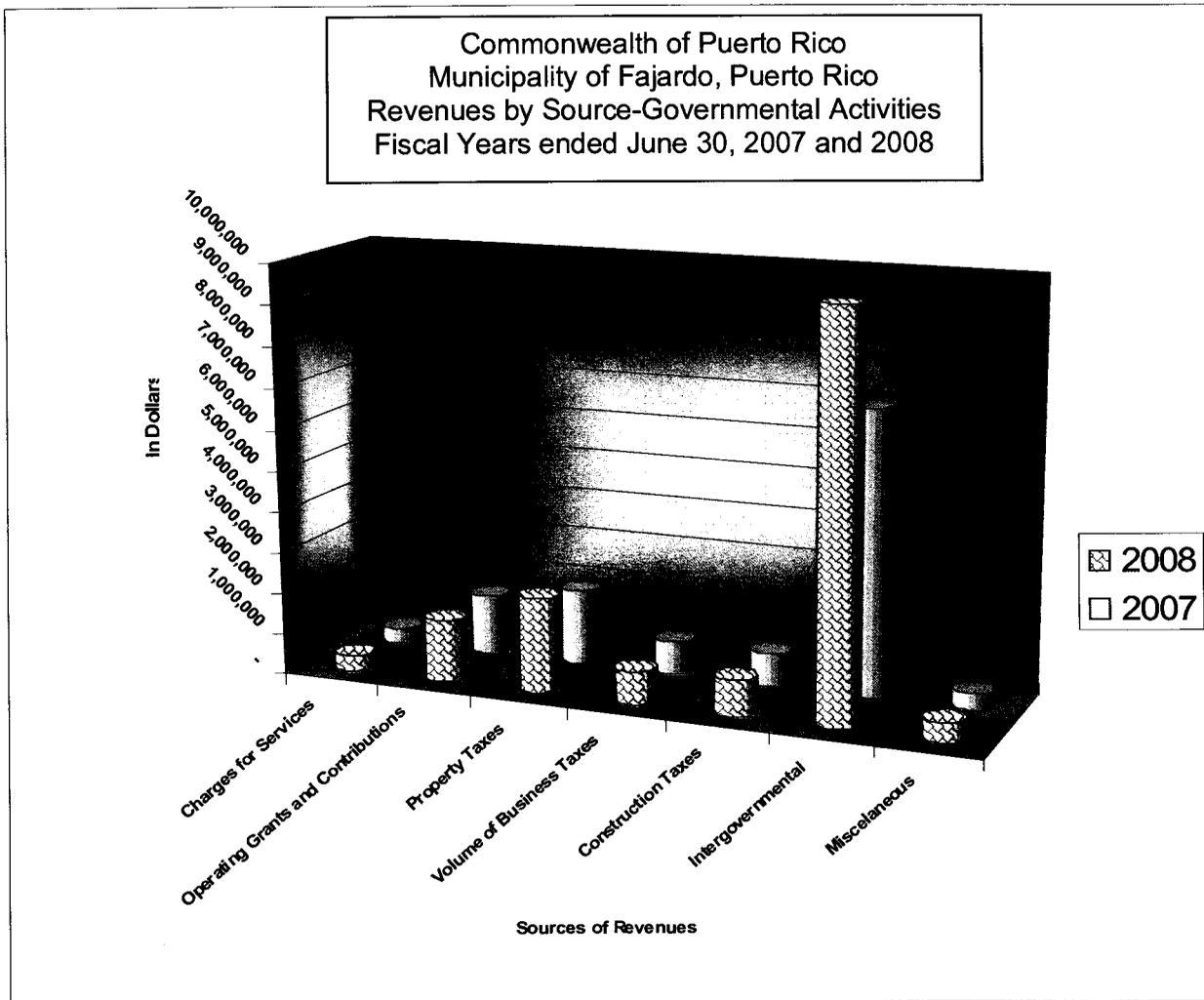
The following table summarizes the changes in net assets for the years ended June 30, 2008 and 2007:

Table 2		
Commonwealth of Puerto Rico Municipality of Fajardo, Puerto Rico Changes in Net Assets For Fiscal Years Ending June 30, 2008		
	2008	2007
Revenues:		
Program Revenues:		
Operating Grants and Contributions ...	\$ 7,807,842	\$ 6,915,779
Capital Grants and Contributions	787,000	3,029,891
General Revenues:		
Property Taxes	11,504,059	11,926,687
Volume of Business Taxes	5,639,390	4,900,359
Sales Taxes	3,313,826	2,288,179
Construction Taxes	962,627	2,048,681
Intergovernmental	4,065,138	3,691,567
Other General Revenues	<u>3,365,753</u>	<u>1,916,003</u>
Total revenues	<u>37,445,635</u>	<u>36,717,146</u>
Expenses:		
General Administration	(13,171,706)	(14,985,902)
Public Safety	(893,755)	(868,914)
Public Works	(3,480,723)	(3,001,400)
Culture and Recreation	(1,494,734)	(579,053)
Health and Sanitation	(2,282,866)	(1,605,421)
Human Services and Welfare	(1,740,812)	(2,327,811)
Solid Waste Disposal	(1,044)	
Public Instruction	(3,863,670)	(3,847,685)
Urban Development	(1,635,907)	(2,213,721)
Interest Costs	<u>(1,192,185)</u>	<u>(1,078,869)</u>
Total expenses	<u>(29,757,402)</u>	<u>(30,148,776)</u>
Changes in net assets	7,688,233	6,568,370
Net assets – beginning	<u>105,676,740</u>	<u>99,108,370</u>
Net assets – ending	<u>\$113,364,973</u>	<u>\$105,676,740</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Figure 1 presents revenues comparison by sources of the governmental activities during the past two years:

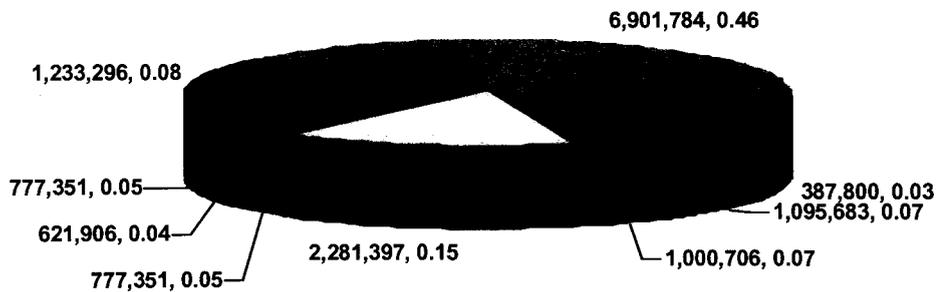
FIGURE 1



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Figure 2 presents expenses by function of the governmental activities during the fiscal year 2007-2008:

FIGURE 2



■ General Administration	■ Sold Waste Desposal	■ Public Safety
■ Human Services and Welfare	■ Public works	■ Urban Development
■ Culture and Recreation	■ Interest Costs	■ Health and Sanitation

Approximately 21% from grants and contributions, 11% of the Municipality's revenues came from intergovernmental, 31% from property taxes, 15% from volume of business tax 9% from sales tax and 13% from other sources. The Municipality's expenses cover a range of services. The largest expenses are general administration with 44%, public instruction with 13%, public works with 12%, health and sanitation with 8%, human services and welfare with 6%, urban development with 5%, and other expenses with 12%. Program revenues of the Municipality covered 29% of total expenses.

With respect to prior year, revenues increased by approximately \$728,489 or 2%, principally on other general revenues such as interest income.

Expenses decreased 1.5% or \$391,374 in comparison with 2007 year.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

The following table focuses on the cost of each of the Municipality's largest functions/programs as well as each functions/program's net cost (total cost less fees generated by the programs and program-specific intergovernmental aid):

TABLE 3

Net Cost of Municipality's Governmental Activities				
Fiscal years ended June 30,				
Functions/Programs	Total Cost of Services		Net Cost of Services	
	2008	2007	2008	2007
General Administration	\$ 13,171,706	\$ 14,985,902	\$ 11,384,953	9,406,063
Public Safety	893,755	868,914	893,755	868,914
Public Works	3,480,723	3,001,400	3,480,723	3,001,400
Culture and Recreation	1,494,734	579,053	1,494,734	579,053
Health and Sanitation	2,282,866	1,605,421	2,282,866	1,605,421
Human Services and Welfare	1,740,812	2,327,811	630,881	1,546,887
Urban Development	1,635,907	2,213,721	142,843	1,811,300
Others	5,056,899	4,566,554	851,805	1,384,068
	<u>\$29,757,402</u>	<u>\$30,148,776</u>	<u>\$21,162,560</u>	<u>\$20,203,106</u>

Some of the cost of governmental activities in 2008 was paid by those who directly benefited from the programs and other governments and organizations that subsidized certain programs with grants and contributions. The \$21,162,560 net cost of services was substantially covered by other general revenues including property, volume of business license taxes, sales tax and intergovernmental.

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

Governmental funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year. For the Fiscal year ended June 30, 2008, the governmental funds reported combined ending fund balances of \$51,298,824, a net increase of \$2,250,340 in comparison with the prior year. This increase was caused primarily by a net change in the general fund due to a reduction in the expenditures. Of total combined fund balances, 7,116,330, constitutes unreserved (deficit) fund balance of general fund. The remainder of fund balance is reserved to indicate that is not available for new spending.

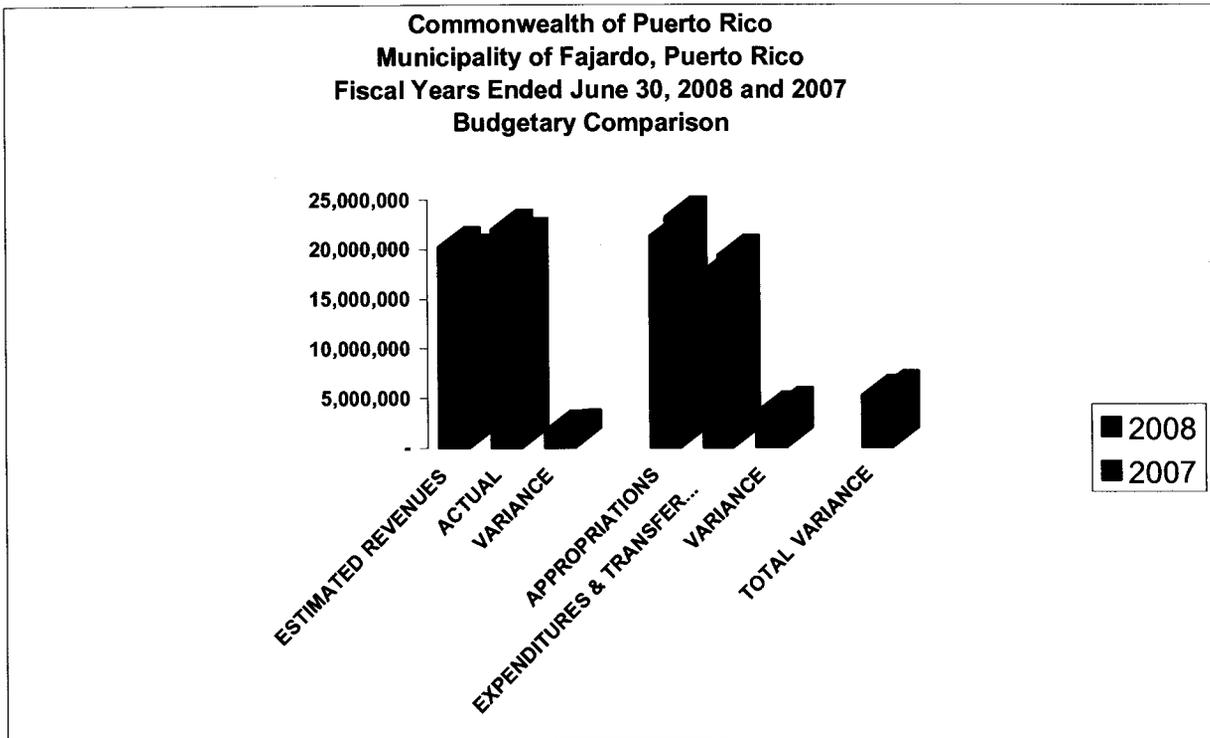
The general fund is the operating fund of the Municipality. Unreserved fund balance of the general fund represents approximately 72% of total ending general fund balance. For the year ended June 30, 2008, the fund balance of the general fund increased by \$4,679,931 when compared with the prior year. The principal component of the net increases is an excess of revenues over expenditures.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

GENERAL FUND BUDGETARY HIGHLIGHTS

The general fund original budget for the fiscal period 2007-2008 presented an increase of 5% with respect to prior year budget. The Municipality did not included as an amendment to the budget the reduction on projected revenues in licenses and permits. Budget expenditures were increased by \$1,043,613, using the budgetary fund balance available (see **Figure 3** below).

FIGURE 3



The Municipality reported less expenditure than appropriations in those functions for payments to purchase of supplies, professional and nonprofessional services, and solid waste disposal.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets

At the end of the fiscal year, the Municipality has invested \$83,875,758 (net of accumulated depreciation) in a broad range of capital assets, including buildings, land, construction in progress and equipment. This amount represents a net increase of \$3,747,728 or 4% from the prior year.

TABLE 4

Commonwealth of Puerto Rico Municipality of Fajardo, Puerto Rico Capital Assets [Net] As of June 30, 2008		
	Governmental Activities	
	2008	2007
NON-DEPRECIABLE ASSETS:		
Land	\$35,275,201	\$34,535,329
Construction in progress	938,286	543,779
Others	765,615	765,615
Depreciable assets:		
Buildings	39,486,296	39,340,057
Equipment and Vehicles	2,729,391	2,621,908
Heavy Equipment	4,626,998	3,942,680
Infrastructure	36,265,608	32,898,485
Total accumulated Depreciation	(36,211,637)	(34,519,823)
Total	\$83,875,758	\$80,128,030

The Municipality acquired a total of \$3,747,728 of capital assets during the fiscal year 2007-2008 as follows:

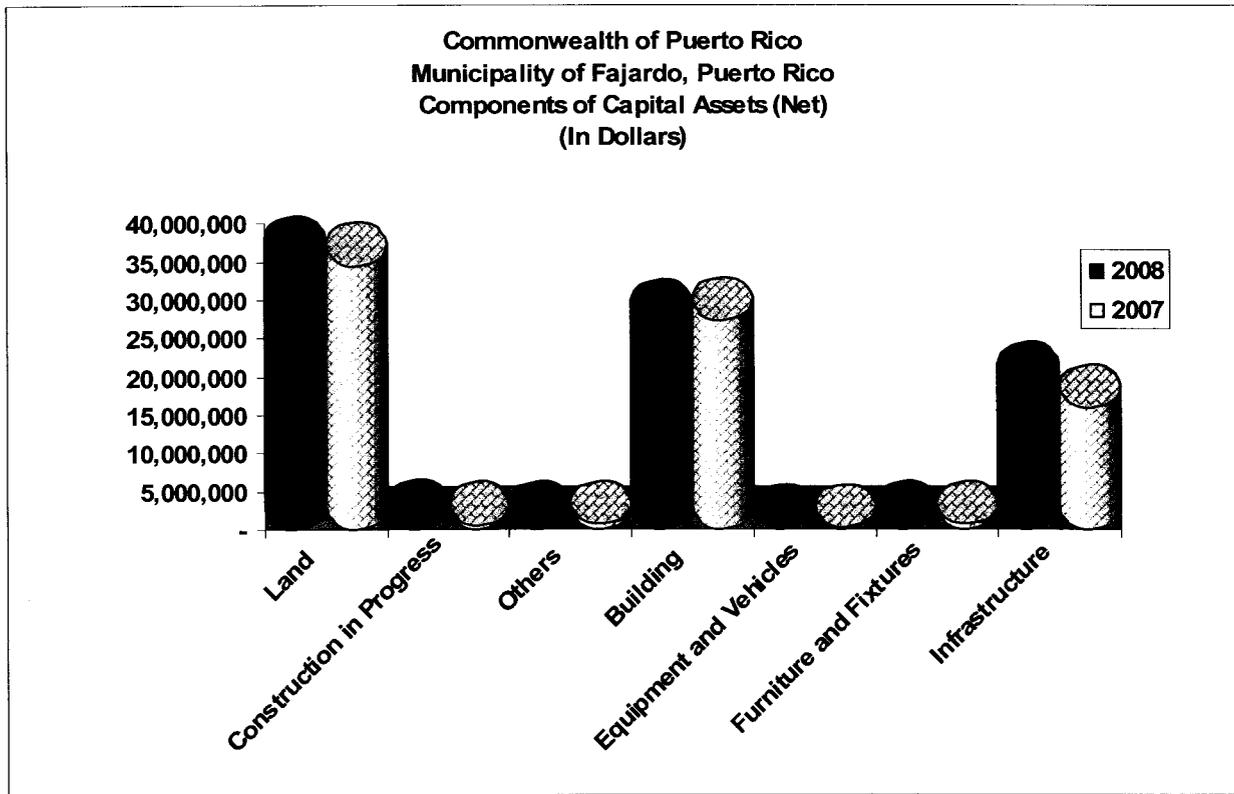
- Construction in Progress – \$394,507
- Acquisition of Equipment and Vehicles – \$791,801
- Buildings and Improvements -146,239
- Land-739,872
- Infrastructure – \$3,367,123

Other projects related to repair and maintenance of roads (not capitalized) was developed during the year 2008.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

Figures 4 below present the components of capital assets during the fiscal years 2008 and 2007:

FIGURE 4



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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Long term debt

At year-end, the Municipality had \$22,325,000 in general and special obligation bonds, a decrease of 2.73% with respect to prior year. The following is a summary of the Municipality's outstanding debt as of June 30, 2008 and 2007:

TABLE 5

Commonwealth of Puerto Rico Municipality of Fajardo, Puerto Rico Outstanding Long-term Debt As of June 30,		
	Governmental Activities	
	2008	2007
General and Special Obligation Bonds	22,325,000	\$ 23,048,000
Property Taxes	219,699	224,402
LIMS	373,449	466,811
Law 146	0	369,162
Others	441,594	431,597
Compensated Absences	3,360,369	3,307,751
Total	26,720,111	\$27,847,723

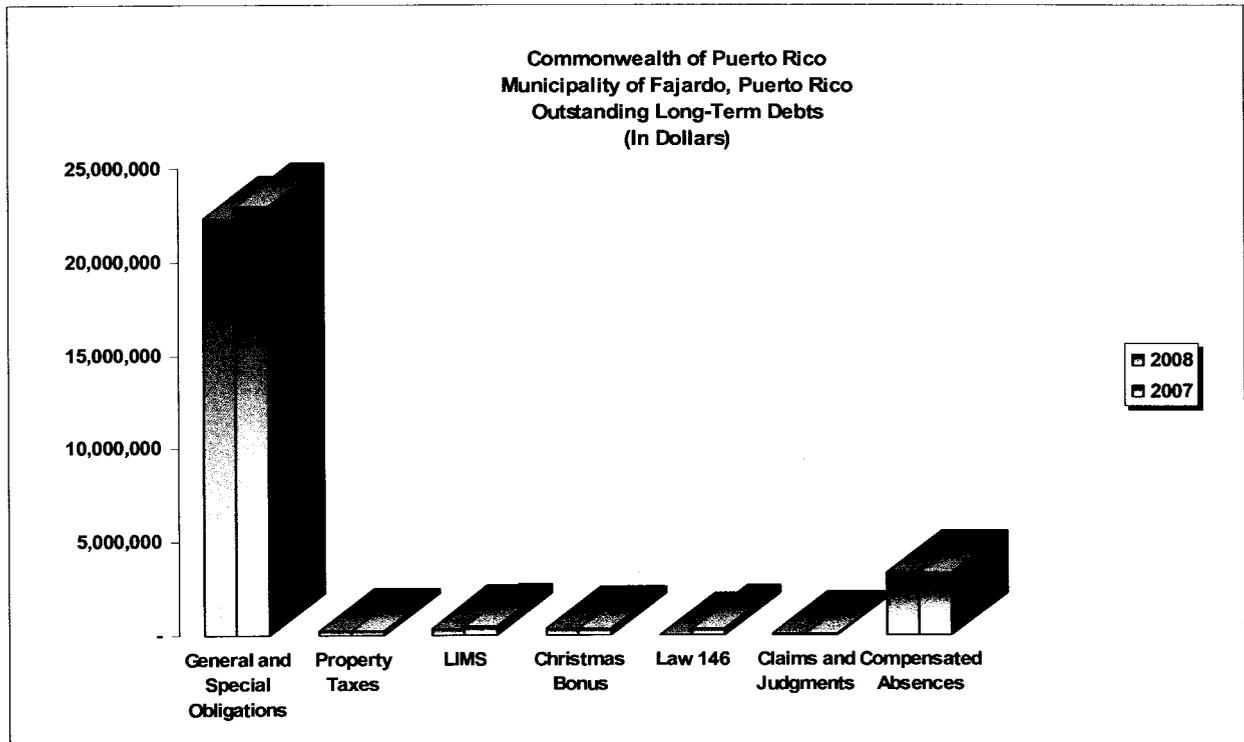
The decrease in the others debts is due to the payment of the Law 146 in full during this fiscal year. More detailed information about the Municipality's long term liabilities is presented in Note 10 and 11 to the financial statements.

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

FOR THE FISCAL YEAR ENDED JUNE 30, 2008

Figure 5 present the components of long-term debts during the fiscal year 2008 and 2007:

FIGURE 5



ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2008-2009 budget. One of these factors is the economy. Among economic areas considered are the population growth estimates, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate now stands at 10.2%, which compares with the Commonwealth rate of 14.1%.

The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2009 are \$18 million, approximately \$600 thousand more than the fiscal year 2008. The Municipality expects an increase in revenues for the next years due to a new sales tax enacted by state legislature and Municipality ordinance during fiscal year 2008-2009. Budgeted expenditures are expected to stabilize accordingly to the projected revenues. Among planned projects, this budget may be adjusted in accordance with economic injection projected when the construction project promoted by the Municipality and others private projects were develop during the year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and creditors with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability for the money it receives. If you have questions about this report or need additional information, contact the Municipality's Finance Department at [(787) 863-1802] or P.O. Box 865, Fajardo, Puerto Rico 00738.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO

STATEMENT OF NET ASSETS
June 30, 2008

	<u>GOVERNMENTAL ACTIVITIES</u>
ASSETS:	
Cash and Investments	\$ 29,513,642
Cash with Fiscal Agent	26,961,453
Receivables (net):	
Property Taxes	48,603
Sales Taxes	249,216
Due from Governmental Units	553,536
Federal Grants	4,816,830
Total Current Assets	<u>62,143,280</u>
Deferred Charges	<u>128,202</u>
Capital Assets:	
Land, Improvement and Construction in Progress	36,979,102
Other Capital Assets [Net of Depreciation]	<u>46,896,656</u>
Total Capital Assets	<u>83,875,758</u>
TOTAL ASSETS	<u>146,147,240</u>
LIABILITIES:	
Accounts Payable and Accrued Expenses	704,987
Accrued Interest	483,893
Due to Governmental Units	132,647
Deferred Revenues	4,740,629
Long-Term Liabilities:	
Due Within One Year	3,610,972
Due in More than One Year	<u>23,109,139</u>
TOTAL LIABILITIES	<u>32,782,267</u>
NET ASSETS:	
Investment in Capital Assets, Net of Related Debt	75,688,196
Restricted for:	
Head Start	1,821,578
Capital Projects	3,250,000
Debt Service	7,665,671
Community Development Projects	1,530,652
Other Purposes	13,024,454
Unrestricted	<u>10,384,422</u>
TOTAL NET ASSETS	<u>\$ 113,364,973</u>

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO

STATEMENT OF ACTIVITIES
For the Fiscal Year Ended June 30, 2008

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenues (See Next Page)
		Charges For Services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
Mayor and Municipal Legislature	\$ 2,577,553	\$ -	\$ -	\$ -	\$ (2,577,553)
General Government	10,594,153	-	1,786,753	-	(8,807,400)
Public Safety	893,755	-	-	-	(893,755)
Public Works	3,480,723	-	-	-	(3,480,723)
Culture and Recreation	1,494,734	-	-	-	(1,494,734)
Health and Sanitation	2,282,866	-	-	-	(2,282,866)
Solid Waste Disposal	1,044	-	-	-	(1,044)
Public Instruction	3,863,670	-	3,919,408	-	55,738
Human Services and Welfare	1,740,812	-	1,109,931	-	(630,881)
Urban Development	1,635,907	-	991,750	787,000	142,843
Interest on Long-Term Debt	1,192,185	-	-	-	(1,192,185)
Total Governmental Activities	\$ 29,757,402	\$ -	\$ 7,807,842	\$ 787,000	(21,162,560)
General Revenues:					
Taxes:					
Property Taxes, levied for General Purposes					8,305,942
Property Taxes, levied for Debt Service					3,198,117
Volume of Business Taxes					5,639,390
Sales Taxes					3,313,826
Construction Taxes					962,627
Intergovernmental					4,065,138
Rent					70,734
Interests					1,702,198
Miscellaneous					1,592,821
Total General Revenues					28,850,793
CHANGES IN NET ASSETS					
8,688,233					
Net Assets – Beginning of Year					105,676,740
NET ASSETS – ENDING OF YEAR					\$ 113,364,973

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO

BALANCE SHEET – GOVERNMENTAL FUNDS
June 30, 2008

	GENERAL FUND	HEAD START FUND	DEBT SERVICE FUND	ARTS CENTER FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS:						
Cash and Investment	\$ 15,294,576	\$ 66,668	\$ -	\$ -	\$ 14,152,398	\$ 29,513,642
Cash with Fiscal Agent	-	-	8,100,961	8,853,170	10,007,322	26,961,453
Receivables:						
Property Taxes	-	-	48,603	-	-	48,603
Sales Tax	-	-	-	-	249,216	249,216
Federal Grants	-	3,663,093	-	-	1,153,737	4,816,830
Due from Other Funds	265,800	-	-	-	1,005,443	1,271,243
Due from Governmental Units	553,536	-	-	-	-	553,536
Total Assets	\$ 16,113,912	\$ 3,729,761	\$ 8,149,564	\$ 8,853,170	\$ 26,568,116	\$ 63,414,523
LIABILITIES AND FUND BALANCES:						
Liabilities:						
Account Payable	\$ 130,823	\$ 333,827	\$ -	\$ -	\$ 240,337	\$ 704,987
Bonds Payable	-	-	904,000	-	-	904,000
Account Interest	-	-	483,893	-	-	483,893
Due to Governmental Units	132,647	-	-	-	-	132,647
Due to Other Funds	1,005,443	265,800	-	-	-	1,271,243
Deferred Revenues:						
Volume of Business Tax	4,460,577	-	-	-	-	4,460,577
Intergovernmental	553,536	-	-	-	-	553,536
Federal Grants	-	2,445,797	-	-	1,159,019	3,604,816
Total Liabilities	6,283,026	3,045,424	1,387,893	-	1,399,356	12,115,699
Fund Balances:						
Reserve For:						
Encumbrances	765,460	-	-	-	-	765,460
Debt Service	-	-	6,761,671	-	-	6,761,671
Other Purposes	1,949,096	684,337	-	8,853,170	25,168,760	36,655,363
Unreserved	7,116,330	-	-	-	-	7,116,330
Total Fund Balances	9,830,886	684,337	6,761,671	8,853,170	25,168,760	51,298,824
Total Liabilities and Fund Balances	\$ 16,113,912	\$ 3,729,761	\$ 8,149,564	\$ 8,853,170	\$ 26,568,116	\$ 63,414,523

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
June 30, 2008

Total Fund Balances – Government Funds (Page 13)		\$ 51,298,824
Amount reported for Governmental Activities in the Statement of Net Assets (Page 11) 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:		
Non Depreciable Capital Assets	\$ 36,979,102	
Depreciable Capital Assets	46,842,685	
Infrastructure Assets	36,265,608	
Accumulated Depreciation	<u>(36,211,637)</u>	
Total Capital Assets		83,875,758
Other Assets used in governmental activities are not financial resources and therefore are not reported in the funds:		
Deferred Charges		128,202
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:		
CDBG	878,967	
Head Start Program	2,445,797	
MRCC Liquidation	383,353	
Christmas Bonus	<u>170,183</u>	
Total Deferred Revenues		3,878,300
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:		
General Obligation Bonds	(21,421,000)	
Property Tax Advances	(1,950)	
Law Number 42 - MRCC	(217,749)	
LIMS - MRCC	(373,449)	
Christmas Bonus	(340,367)	
Claims and Judgments	(101,227)	
Compensated Absences	<u>(3,360,369)</u>	
Total Long-Term Liabilities		<u>(25,816,111)</u>
Total Net Assets of Governmental Activities (Page 11)		<u>\$ 113,364,973</u>

See accompanying Notes to Basic Financial Statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE – GOVERNMENTAL FUNDS
For the Fiscal Year Ended June 30, 2008

	GENERAL FUND	HEAD START FUND	DEBT SERVICE FUND	ARTS CENTER FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
REVENUES:						
Property Taxes	\$ 8,305,942	\$ -	\$ 3,198,117	\$ -	\$ -	\$ 11,504,059
Volume of Business Taxes	5,639,390	-	-	-	-	5,639,390
Sales Taxes	-	-	-	-	-	-
Federal Assistances	-	3,915,129	-	-	3,313,826	3,313,826
Intergovernmental	3,676,787	-	-	-	2,249,447	6,164,576
Licenses and Permits	962,627	-	-	-	2,573,753	6,250,540
Rent	70,734	-	-	-	-	962,627
Interests	1,702,198	-	-	-	-	70,734
Miscellaneous	1,576,144	-	-	-	-	1,702,198
					16,677	1,592,821
Total Revenues	21,933,822	3,915,129	3,198,117	-	8,153,703	37,200,771
EXPENDITURES:						
Current:						
Mayor and Municipal Legislature	2,547,899	-	-	-	29,654	2,577,553
General Government	5,993,616	-	-	-	3,922,559	9,916,175
Public Safety	826,083	-	-	-	-	826,083
Public Works	2,569,002	-	-	-	-	-
Culture and Recreation	1,315,091	-	-	-	218,077	2,787,079
Health and Sanitation	1,690,611	-	-	-	95,052	1,410,143
Public Instruction	-	3,863,670	-	-	593,299	2,283,910
Human Services and Welfare	1,314,361	-	-	-	-	3,863,670
Urban Development	26,713	-	-	-	426,451	1,740,812
Capital Outlay	183,054	-	-	-	1,372,340	1,399,053
Debt Service:					5,256,488	5,439,542
Principal	-	-	1,514,226	-	-	1,514,226
Interest and Other Charges	-	-	1,192,185	-	-	1,192,185
Total Expenditures	16,466,430	3,863,670	2,706,411	-	11,913,920	34,950,431
Excess of Revenues Over (Under) Expenditures	5,467,392	51,459	491,706	-	(3,760,217)	2,250,340
OTHER FINANCING SOURCES (USES):						
Transfer – In	-	-	527,461	-	260,000	787,461
Transfer – Out	(787,461)	-	-	-	-	(787,461)
Total Other Financing Sources and Uses	(787,461)	-	527,461	-	260,000	-
Net Change in Fund Balance	4,679,931	51,459	1,019,167	-	(3,500,217)	2,250,340
Fund Balance – Beginning	5,150,955	632,878	5,742,504	8,853,170	28,668,977	49,048,484
FUND BALANCE – ENDING	\$ 9,830,886	\$ 684,337	\$ 6,761,671	\$ 8,853,170	\$ 25,168,760	\$ 51,298,824

*Call
5/1/09*

See accompanying Notes to Basic Financial Statements.

Net Change in Fund Balances – Government Funds (Page 15)		\$ 2,250,340
Amount reported for Governmental Activities in the Statement of Activities (Page 12) are different because:		
Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. In the current period, these amounts are:		
Capital Assets	\$ 5,439,542	
Depreciation Expense	<u>(1,691,814)</u>	
Excess of Capital Assets over Depreciation Expense		3,747,728
Revenues in the Statement of Activities that do not provide current financial resources are reported as revenues in the funds:		
Property Taxes Final Liquidation	383,353	
Christmas Bonus	4,999	
Head Start Program	4,279	
Community Development Block Grant	<u>(147,767)</u>	
Total of Revenues		244,864
Repayment of long-term principal is expenditure in the governmental funds, but issuing debt reduced Long-Term Liabilities in the Statement of Net Assets. In the current period repayments were		
		1,514,226
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:		
Bond Issue Costs Amortization	(6,310)	
Christmas Bonus	(9,997)	
Increase in Compensated Absences	<u>(52,618)</u>	
Total Additional Expenses		<u>(68,925)</u>
Change in Net Assets of Governmental Activities (Page 12)		\$ <u>7,688,233</u>

NOTE 1 FINANCIAL REPORTING ENTITY

The **Municipality of Fajardo, Puerto Rico (Municipality)** was founded in the year 1775, and operates as a governmental unit of the Commonwealth of Puerto Rico, under the Law Number 81 of August 30, 1991, known as "Autonomy Municipalities Law of the Commonwealth of Puerto Rico". The governmental system of the **Municipality** is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of the Commonwealth of Puerto Rico. The legislative body consists of 14 Legislators also elected in the general elections of Puerto Rico for a four-year period.

The **Municipality** provides services such as: health, public works, sanitation, aids and services to low-income and elderly citizens, public safety, housing and urban development, culture and recreation, planning, zoning and other general and administrative services. As a government entity, the **Municipality** is exempt from both federal and state taxes.

The accounting policies of the **Municipality** conform to 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. The following is a summary of the more significant of such policies.

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, as amended by GASBS No. 39, *Determining Whether Certain Organizations Are Component Units – an amendment of GASB Statement No. 14*.

GASBS No. 39 provided additional guidance to determine whether certain organization for which the primary government is not financially accountable should be reported as components units. A legally separate, tax-exempt organization should be discretely presented as a component unit if all of the following criteria are met: (a) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (b) the primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (c) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

There are two methods of presentation of the component unit in the financial statements: blending – the financial data of the component unit's balances and transactions in a manner similar to the presentation of the **Municipality's** balance; and discrete – presentation of the component unit's financial data in column separate from the **Municipality's** balances and transactions.

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 and business type activities, each major fund, and the aggregate remaining fund information of the **Municipality**, as of June 30, 2008, and the respective changes in financial position, where applicable, thereof for the fiscal year then ended.

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES

A. Financial Statement Presentation

The basic financial statements include both government-wide (based on the **Municipality** as a whole) and fund financial statements. Both the government-wide and fund financial statements (within the basic financial statements) categorize primary activities as either governmental or business type.

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 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. Business-type activities are not reported seen the **Municipality** don't have such activities.

The focus of the *Statement of Net Assets* is designed to be similar to bottom line results for the **Municipality's** governmental activities and business type activities. This statement combines and consolidates governmental fund's current financial resources (short-term spendable resources) with capital assets and long-term obligations. The *Statement of Net Assets* presents the reporting entities' assets and liabilities, with the difference reported as net assets.

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 *Statement of Activities* demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Governmental Funds Financial Statements

The fund financial statements [the *Balance Sheet*, the *Statement of Revenues, Expenditures, and Changes in Fund Balance*] provide information about the **Municipality's** funds. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. Non-major funds are summarized into a single column.

continue

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES
(continuation)

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. 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 different measurement focus and basis of accounting than the government-wide statements, reconciliation is presented and 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.

B. Measurement Focus and Basis of Accounting

Government-wide Financial Statements

The government-wide financial statements 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. Property taxes are recognized as revenues in the year for which they are levied. Grant and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental Funds Financial Statements

The governmental funds financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purposes, the **Municipality** considers revenues to be available if they are collected within sixty (60) days of the end of the current fiscal period. Expenditures generally are recorded when liability is incurred, as under accrual accounting. However, expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, volume of business taxes, licenses and permits, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the **Municipality**.

In applying the "susceptible to accrual" concept to intergovernmental revenues (federal grants) pursuant to GASBS No. 33, *Accounting and Financial Reporting for Nonexchange Transactions* (the **Municipality**

may act as either provider or recipient), the provider should recognize liabilities and expenses and the recipient should recognize receivables and revenue when the applicable eligibility requirements including time requirements, are met. Resources transmitted before the eligibility requirements are met should, under most circumstances, be reported as advances by the provider and deferred revenue by the recipient.

There are essentially two types of revenue. For the majority of grants, moneys 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 recognized when the related liability is incurred, as under accrual accounting. The exceptions to this general rule are the compensated absences and claims and judgments, if any, that are recorded only when payment is due.

The **Municipality** reports the following major governmental 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.

Head Start Fund – This is the fund used to account for all transactions of the Head Start Program. The objectives to this program are to provide comprehensive health, educational, nutritional, social and other developmental services primarily to economically-disadvantaged pre-school children and infants and toddlers so that the children will attain school readiness.

Debt Service Fund – This is used to account for the accumulation of resources for, and the payment of long-term debt principal and interests.

Arts Center Fund – This fund is used to account for the construction of an Arts Center.

The non-major funds are combined in a single column in the fund financial statements.

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

C. Stewardship, Compliance, and Accountability

Budgetary Information

The **Municipality's** annually adopts the Budget Resolution for all operating funds of the **Municipality** except for certain restricted accounts 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.

continue

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES
(continuation)

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 a supplemental appropriation(s). During the year, several supplemental appropriations were necessary.

Encumbrances outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent year.

The **Municipality** follows these procedures, in accordance with law, in order to establish the budgetary data reflected in the Budgetary Comparison Statement – General Fund:

Original Budget

1. Prior of May 15 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 to be effective on July 1.

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 Statement, is presented on the budgetary basis to enhance comparability.

Final Budget

The final budgetary data presented in the Budgetary Comparison Statement – General Fund reflects the following changes to the original budget:

1. Certain annual appropriations are budgeted on a project basis. If such projects are not completed at the end of the fiscal year, unexpended appropriations, including encumbered funds, and unexpended grant appropriations, are carried forward to the following year. In certain circumstances, other regular annual appropriations may be carried forward after appropriate approval. Annually appropriated funds, not authorized to be carried forward, lapse at the end of the fiscal year. Appropriations carried

forward from the prior year are included in the final budgetary data.

2. Appropriations may be adjusted during the year with the approval of the Mayor and the Municipal Legislature, e.g. supplemental appropriations. Additionally, the Mayor is authorized to make certain transfer of surplus within the departments. Such adjustments are reflected in the final budgetary data.

The Annual Appropriation Ordinance adopts the budget at the character level of expenditure within departments. As described above, the Mayor is authorized to make certain transfers of appropriations within departments. Accordingly, the legal level of budgetary control by the Municipal Legislature is the department Level.

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. Interfund transactions of the General Fund are not included in the budgetary basis.
3. Certain accrued liabilities and other debts are not included in the budgetary basis.
4. Certain revenues susceptible to accrual, i.e., both measurable and available, are not included in the budgetary data.

The Special Revenue Fund has not been included in the budgetary comparison because balances are not budgeted. Also the budget prepared for the Federal Financial Awards Programs included in the Capital Projects and Special Revenue Funds is based on a program period which is not necessarily the same fiscal year. Accordingly, it's not practical to present an annual comparison of budget for such programs.

D. Cash and Investment, and Cash with Fiscal Agent

The Director of Finance 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.

Cash with fiscal agent in the Debt Service Fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the **Municipality's** debt service, as established by law. Cash with fiscal agent in other governmental funds consists of undisbursed proceeds of certain bonds and notes issued for the acquisition and construction of major capital improvements, or grants which are maintained in a cash custodian account by the Government Development Bank of the Commonwealth of Puerto Rico. This 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.

continue

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES
(continuation)

E. Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statement as "interfund balances".

Receivable are shown net of an allowances for uncollectible, which are determined upon past collection experience and current economic conditions. Intergovernmental receivables in the general fund represent mostly property tax accounts that are levied by Municipal Revenue Collection Center (MRCC), a governmental entity created by the Commonwealth of Puerto Rico, from grant and contributions from Federal Government, and state appropriations.

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

F. Inventories

The **Municipality** used the purchase method to account for the purchases office and printing supplies, gasoline, oil and other expendable supplies held for consumption. This method records items as expenditures, in the appropriate fund, when they are acquired and, accordingly, the inventory is not recorded in the basic financial statements.

G. Capital Assets

Capital assets, which include land, buildings and improvement, machinery and equipment, motor vehicles, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets, other than infrastructure assets, are defined by the government as assets with an initial, individual cost of more than \$500 (amount not rounded) and an estimated useful life in excess of two years. 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. The government reports infrastructure assets on a network and subsystem basis. Accordingly, the amounts spent for the construction or acquisition of infrastructure assets are capitalized and reported in the government-wide financial statements regardless of their amount.

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by governmental activities) the government chose to include all such items regardless of their acquisition date or amount.

The government was able to estimate the historical cost for the initial reporting of these assets through back trending (i.e., estimating the current replacement cost of the infrastructure to be capitalized and using

an appropriate price-level index to deflate the cost to the acquisition year or estimated acquisition year). As the government constructs or acquires additional capital assets each period, including infrastructure assets, they are capitalized and reported at historical cost. The reported value excludes normal maintenance and repairs which are essentially amounts spent in relation to capital assets that do not increase the capacity or efficiency of the item or extend its useful life beyond the original estimate. In the case of donations the government values these capital assets at the estimated fair value of the item at the date of its donation.

Capital outlay is recorded as expenditures of the General Fund and other governmental funds and as assets in the government-wide financial statements to the extent the **Municipality** capitalization threshold is met. Interest incurred during the construction phase of the capital assets of business-type activities is reflected in the capitalized value of the asset acquired under capital leases is included in depreciation. Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

CAPITAL ASSETS	YEARS
Buildings	50
Improvement Other Than Buildings	50
Infrastructure	10-50
Motor Vehicles	5
Machinery and Equipments	5-10

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

H. 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.

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES
(continuation)

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, including its share of social security and Medicare payments made on behalf of the employees in the accrual for vacation and sick leave pay. All vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements. 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 (see Note 11 on page 25).

I. Risk Financing

The **Municipality** carries commercial insurance to cover property and 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. Also, principal officials of the **Municipality** are covered under various surety bonds. Cost of insurance allocated to the **Municipality** and deducted from the gross property tax collections by the MRCC for the year ended June 30, 2008 amounted to approximately \$443,068. The current insurance policies have not been cancelled or terminated. In addition, MRCC deducted approximately \$308,980 for workers compensation insurance covering all municipal employees for the same period.

J. Long-Term Obligations, Bonds Issuance Costs, Premiums and Discounts

The liabilities reported in the government-wide financial statements include the general and special obligation bonds, long-term notes, other long-term liabilities (e.g., vacation, sick leave, claims and judgments, and long-term liabilities to other governmental entities and third parties. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount.

In the fund financial statements, governmental fund types recognize bond premiums and discounts as other financing sources and uses, respectively, and bond issuance costs as debt service expenditures. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

K. Fund Equity/Net Assets

Reservations of Fund Equity

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditures or (2) legally segregated for a specific future use. Following is a brief description of the nature of certain reserves.

- **Reserve for Encumbrances** – Encumbrances are recorded as reservations of fund balances because they do not constitute expenditures or liabilities. In certain other governmental funds, this accounting treatment results in a deficit unreserved fund balance.

This deficiency is carried forward to the next fiscal year where it is applied against estimated revenues in the year the commitments are expended.

- **Reserve for Debt Service** – The fund balance of the debt service funds is reserved for the payment of debt service in the subsequent years.
- **Reserve for Capital Projects** – Certain assets, primarily cash and investments, and cash with fiscal agent to be invested in capital projects.
- **Reserve for Other Purposes** – Certain assets, primarily cash and investments of grants and contributions that are authorized to be carried over and expended in the ensuing year.

Restricted Net Assets

The governmental-wide and proprietary funds financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted, and unrestricted.

- **Invested in Capital Assets, Net of Related Debt** – These consists of capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and amortization, and the outstanding balances for debt that are attributable to the acquisition, construction, or improvement of these assets reduce the balance in this category.
- **Restricted Net Assets** – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- **Unrestricted Net Assets** – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

L. Interfund Transactions

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

Interfund Transfers – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds.

Intra-Entity Transactions – Advances between funds are also presented as amounts due to and due from other funds.

continue

NOTE 2 SUMMARIES OF SIGNIFICANT ACCOUNTING POLICIES
(continuation)

However, these transfers and related amounts receivables and payables are considered internal balances and activities that have been eliminated in the government-wide financial statements.

M. 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.

O. 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.

N. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board (GASB) issued the following pronouncement that does not apply to the **Municipality**:

GASB Statement No. 49, *Pollution Remediation*. This Statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of *existing* pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the document excludes *pollution prevention* or *control* obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and postclosure care and nuclear power plant decommissioning.

This Statement are effective for financial statements for periods beginning after December 15, 2007, with measurement of pollution remediation liabilities required at the beginning of that period so that beginning net assets can be restated. However, governments that have sufficient objective and verifiable information to apply the expected cash flow technique to measurements in prior periods are required to apply the provisions retroactively for all such prior periods presented.

GASB Statement No. 51, *Intangible Assets*. This Statement requires that an intangible asset be recognized in the statement of net assets only if it is considered identifiable. Additionally, this Statement establishes a specified-conditions approach to recognizing intangible assets that are internally generated. Effectively, outlays associated with the development of such assets should not begin to be capitalized until certain criteria are met. Outlays incurred prior to meeting these criteria should be expensed as incurred. This Statement also provides guidance on recognizing internally generated computer software as an intangible asset. This Statement is effective for financial statements for

periods beginning after June 15, 2009. The provisions of this Statement generally are required to be applied retroactively. For governments that were classified as phase 1 or phase 2 governments for the purpose of implementing Statement 34, retroactive reporting is required for intangible assets acquired in fiscal years ending after June 30, 1980, except for those considered to have indefinite useful lives as of the effective date of this Statement and those that would be considered internally generated. Retroactive reporting of these intangible assets by phase 3 governments is encouraged but not required. Retroactive reporting is not required but is permitted for intangible assets considered to have indefinite useful lives as of the effective date of this Statement and those considered to be internally generated.

GASB Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. This Statement establishes consistent standards for the reporting of land and other real estate held as investments by essentially similar entities. It requires endowments to report their land and other real estate investments at fair value. Governments also are required to report the changes in fair value as investment income and to disclose the methods and significant assumptions employed to determine fair value, and other information that they currently present for other investments reported at fair value. This Statement is effective for financial statements for periods beginning after June 15, 2008.

GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. Statement 53 is intended to improve how state and local governments report information about derivative instruments—financial arrangements used by governments to manage specific risks or make investments—in their financial statements. The Statement specifically requires governments to measure most derivative instruments at fair value in their financial statements that are prepared using the economic resources measurement focus and the accrual basis of accounting. The guidance in this Statement also addresses hedge accounting requirements and is effective for financial statements for reporting periods beginning after June 15, 2009, with earlier application encouraged.

NOTE 3 CASH AND INVESTMENTS

Certificates of Deposit

Investments consist of certificates of deposit. The **Municipality's** cash and investments at year-end were entirely covered by the Federal Deposit Insurance Corporation (FDIC) coverage, up to a maximum of \$250,000 in each bank, and the excess by collateral provided by the banks and held by the Puerto Rico Treasury Department pursuant the applicable laws and regulations. Cash with fiscal agent is maintained in interest bearing accounts in the Government Development Bank of Puerto Rico and is not collateralized.

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Commonwealth of Puerto Rico. The **Municipality** is also allowed to invest in bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the federal and Commonwealth laws.

continue

NOTE 3 CASH AND INVESTMENTS (continuation)

During the year, the **Municipality** invested its funds in interest bearing bank accounts and short-term certificates of deposit. As June 30, 2008 the market value of investments approximated its carrying value as follow:

CERTIFICATE OF DEPOSIT ISSUED BY	PRINCIPAL NUMBER	INTEREST AMOUNT	RATE	EXPIRATION DATE
Popular Bank of Puerto Rico	1110000048	\$ 2,600,000	3.65%	07/05/08
Popular Bank of Puerto Rico	1110000049	6,000,000	3.65%	07/05/08
Popular Bank of Puerto Rico	1110000050	600,000	3.00%	07/21/08
EuroBank of Puerto Rico	2805000509	<u>1,500,000</u>	3.65%	07/05/08
		<u>\$ 10,700,000</u>		

Custodial Credit Risk Related to Deposits

Custodial credit risk for cash and investments is the risk that, in the event of the failure of a depository financial institution, the **Municipality** will not be able to recover its cash and investments or will not be able to recover collateral securities that are in the possession of an outside party. Pursuant to the Investment Guidelines for the Commonwealth adopted by GDB, the **Municipality** may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, banker's acceptance, or in pools of obligations of the municipalities of Puerto Rico, among others.

The **Municipality** maintains its cash deposits in commercial banks located in Puerto Rico. Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal deposit insurance. All securities pledged as collateral by the **Municipality** are held by the Secretary of Treasury of Puerto Rico in the **Municipality's** name. The following tables presented below discloses the level of custody risk assumed by the **Municipality** based upon how its deposits were insured or secured with collateral at June 30, 2008:

Category 1: Insured or collateralized with securities held by the Secretary of Treasury agent's in the **Municipality's** name.

Category 2: Collateralized with securities held by the pledging financial institution's trust department or its agents in the **Municipality's** name.

Category 3: Uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent by not in the **Municipality's** name.

The investments are distributed by the amounts of \$4,700,000 to the General Fund and \$6,000,000 to the Special Revenue Fund.

As of June 30, 2008, the **Municipality's** custodial credit risk was approximately \$12.4 million, which is the bank balance of

cash deposited at the Government Development Bank of Puerto Rico (GDB). These deposits are exempt from the collateral requirement established by the Commonwealth.

NOTE 4 DUE FROM GOVERNMENTAL UNITS

The due from agencies for the fiscal year ended June 30, 2008, corresponds to the Puerto Rico Treasury Department (Christmas Bonus) for \$170,183 and Property Tax Final Liquidation from MRCC for \$383,353.

NOTE 5 INTERFUND TRANSFER AND BALANCES

Transfers are indicative of funding for capital projects or debt service, and subsidies of various operations.

INTERFUND TRANSFERS WITHIN THE GOVERNMENTAL FUNDS			
SOURCES	TRANSFER TO	AMOUNT	PURPOSE
General Fund	Debt Service Fund	\$ 527,461	Debt Payment
General Fund	Other Fund	<u>260,000</u>	Specific Project Funding
Total		<u>\$ 787,461</u>	

NOTE 6 INTERFUND RECEIVABLE AND PAYABLE BALANCES

Interfund receivables and payables at June 30, 2008 are summarized as follows:

INTERFUND RECEIVABLE	INTERFUND PAYABLE	AMOUNT
General	Head Start Fund	\$ 265,800
Other Fund	General Fund	<u>1,005,443</u>
TOTAL		<u>\$ 1,271,243</u>

	CATEGORY			CARRYING AMOUNT	BANK BALANCE
	1	2	3		
Deposits in Commercial Banks	\$ 44,059,291	\$ -	\$ -	\$ 44,059,291	\$ 44,059,446
Deposits in Governmental Banks	-	-	12,415,804	12,415,804	12,415,774
Total	<u>\$ 44,059,291</u>	<u>\$ -</u>	<u>\$ 12,415,804</u>	<u>\$ 56,475,095</u>	<u>\$ 56,475,220</u>
Reconciliation to Government-Wide Statement of Net Assets:					
	UNRESTRICTED	RESTRICTED	TOTAL		
Carrying amount of deposits in Commercial Banks	\$ 15,294,576	\$ 28,764,715	\$ 44,059,291		
Carrying amount of deposits in Governmental Bank	-	12,415,804	12,415,804		
Total	<u>\$ 15,294,576</u>	<u>\$ 41,180,519</u>	<u>\$ 56,475,095</u>		

continue

NOTE 7 DUE TO OTHER GOVERNMENTAL UNITS

As of June 30, 2008, balance due to other governmental units of the General Fund for services rendered to the **Municipality**, consists of the following:

	AMOUNT
PR Water and Sewer Authority	\$ 9,490
Retirement System Administration	\$ 119,550
General Service Administration	3,607
Total Due to Governmental Units	\$ 132,647

NOTE 8 DEFERRED REVENUES

Governmental funds report *deferred revenues* in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of *deferred revenue* and *unearned revenue* reported in the governmental funds were as follows:

	UNAVAILABLE	UNEARNED
Volume of Business Taxes	\$ -	\$ 4,460,577
Other Governmental Funds	1,159,019	-
MRCC Liquidation	383,353	-
Head Start	2,445,797	-
Christmas Bonus	170,183	-
Total Deferred/Unearned Revenue	\$ 4,158,352	\$ 4,460,577

NOTE 9 CAPITAL ASSETS

Capital Assets activities for the fiscal year ended June 30, 2008 was as follows:

DESCRIPTION	BALANCE		ADJUSTMENT	INCREASE	DECREASE	BALANCE	
	JULY 1, 2007					JUNE 30, 2008	
Non-Depreciable Capital Assets:							
Land	\$ 34,535,329	\$ -	\$ -	\$ 739,872	\$ -	\$ 35,275,201	
Construction in Progress	543,779	-	-	394,507	-	938,286	
Others	765,615	-	-	-	-	765,615	
Total Non-Depreciable Capital Assets	35,844,723	-	-	1,134,379	-	36,979,102	
Depreciable Capital Assets:							
Buildings and Improvements	39,340,057	-	-	146,239	-	39,486,296	
Infrastructure	32,898,485	-	-	3,367,123	-	36,265,608	
Machinery and Equipment	3,942,680	-	-	684,318	-	4,626,998	
Motor Vehicles	2,621,908	-	-	107,483	-	2,729,391	
Total Depreciable Capital Assets	78,803,130	-	-	4,305,163	-	83,108,293	
Less Accumulated Depreciation:							
Buildings and Improvements	(12,047,147)	-	-	(362,414)	-	(12,409,561)	
Infrastructure	(16,876,628)	-	-	(518,619)	-	(17,395,247)	
Machinery and Equipment	(3,254,383)	-	-	(696,733)	-	(3,951,116)	
Motor Vehicles	(2,341,665)	-	-	(114,048)	-	(2,455,713)	
Total Accumulated Depreciation	(34,519,823)	-	-	(1,691,814)	-	(36,211,637)	
Total Depreciable Capital Assets (Net)	44,283,307	-	-	2,613,349	-	46,896,656	
CAPITAL ASSETS, NET	\$ 80,128,030	\$ -	\$ -	\$ 3,747,728	\$ -	\$ 83,875,758	

Depreciation expenses were charged to governmental functions/programs as follows:

	AMOUNT
General Government	\$ 609,053
Public Safety	67,672
Public Works	693,644
Culture and Recreation	84,591
Urban Development	236,854
Total Depreciation Expenses	\$ 1,691,814

continue

NOTE 10 GENERAL LONG-TERM DEBTS

A. General Obligations Bonds

The principal long-term obligations of the **Municipality** are general obligation bonds issued to finance the construction and improvements of public facilities. The **Municipality's** obligations long-term debt retirements are appropriated and paid from resources accumulated in the Debt Service Fund (See Note 11).

General obligations bonds as of June 30, 2008, are comprised of the following individual issues:

B. Other Long-Term Debts

Property Taxes – Treasury Department

This amount represents the excess of advance property taxes over collection previously administered by Puerto Rico Treasury Department. On July 1, 2002, the enacted Law Number 29, authorized that part of the excess of revenue from LOTO should be use to amortized this debt. Annually the Treasury Department should notify to the **Municipality** the amount applied to the debt.

Borrowing from MRCC

On July 1, 2002, the **Municipality** entered into a repayment agreement with the GDB and MRCC to repay the uncollectible property tax sale authorized by the enacted Law Number 42. The original debt was \$235,722 to be paid during 30 years plus annual interest of 6.1875%.

On November 28, 2001, the **Municipality** entered into a repayment agreement with the GDB and MRCC to pay for the proportional debt to cover the Land Information Management System (LIMS), system established by MRCC with the capacity to maintaining cadastre and photos of all real property of Puerto Rico. The original debt was \$892,993 to be paid during 10 years plus annual interest of 5.95%.

Christmas Bonus

This amount represents the estimated accrued Christmas bonus accumulated as of June 30, 2008 and payroll related benefits, representing the benefit to employees to be paid during the first week of December 2008.

Claims and Judgments

This amount represents the amount accrued for possible claims arising from litigations.

Compensated Absences

This amount represents the estimated accrued vacation benefits, accrued sick leave benefits and payroll related benefits, representing the **Municipality's** commitment to fund such costs from future operations.

Type of Obligation and Purpose	Maturity Date	Interest Rate	Amount
General Obligation Bonds:			
\$11,130,000, Series 1997-98 - General Construction	2016	5.19% to 6.34%	\$ 7,620,000
\$14,440,000, Series 2006-07 - General Construction	2031	5.59% to 7.00%	14,440,000
\$370,000, Series 1994-95 - General Construction	2019	6.106% to 8.206%	265,000
Total General Obligation Bonds			\$ 22,325,000

Following are the Other Long-Term Debts:

DESCRIPTION	BALANCE		RETIREMENTS AND ADJUSTMENT	BALANCE
	JULY 1, 2007	NEW ISSUES		
Property Taxes-Treasury Dept.	\$ 2,922	\$ -	\$ (972)	\$ 1,950
Law Number 42 - MRCC	221,480	-	(3,731)	217,749
Law Number 146 - MRCC	369,162	-	(369,162)	-
LIMS - MRCC	466,811	-	(93,362)	373,449
Christmas Bonus	330,370	340,367	(330,370)	340,367
Claims and Judgments	101,227	-	-	101,227
Compensated Absences	3,307,751	52,618	-	3,360,369
TOTAL	\$ 4,799,723	\$ 392,985	\$ (797,597)	\$ 4,395,111

C. Changes in General Long-Term Debts

The following is a summary of changes in long-term debts for the year ended June 30, 2008:

DESCRIPTION	BALANCE		RETIREMENTS AND ADJUSTMENTS	BALANCE	AMOUNTS DUE WITHIN ONE YEAR	AMOUNTS DUE AFTER NEXT YEAR
	JULY 1, 2007	NEW ISSUES				
General	\$ 22,905,000	\$ -	\$ (580,000)	\$ 22,325,000	\$ 904,000	\$ 21,421,000
Special	143,000	-	(143,000)	-	-	-
Others Debts	4,799,723	392,985	(797,597)	4,395,111	2,706,972	1,688,139
TOTAL	\$ 27,847,723	\$ 392,985	\$ (1,520,597)	\$ 26,720,111	\$ 3,610,972	\$ 23,109,139

D. Debt Compliance

There are a number of limitations and restrictions contained in the various bond indentures. The **Municipality** believes it is in compliance with all significant limitations and restrictions.

NOTE 10 GENERAL LONG-TERM DEBTS (continuation)

The annual requirements to amortize the long-term debts outstanding as of June 30, 2008 are as follows:

a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the MRCC remits to the **Municipality** property taxes advances, which are less than the tax actually collected, a receivable from the MRCC is

YEAR ENDING JUNE 30,	General Obligation Bonds		Other Long-Term Obligations		TOTAL	
	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL PAYMENT	INTEREST PAYMENT	PRINCIPAL	INTEREST
2009	\$ 904,000	\$ 1,194,385	\$ 2,706,972	\$ 24,182	\$ 3,610,972	\$ 1,218,567
2010	1,004,000	1,407,817	110,166	27,955	1,114,166	1,435,772
2011	1,069,000	1,343,229	115,804	21,351	1,184,804	1,364,580
2012	1,136,000	1,274,076	62,915	14,347	1,198,915	1,288,423
2013	1,208,000	1,199,978	5,060	12,319	1,213,060	1,212,297
2014-2018	6,228,000	4,706,450	30,486	56,404	6,258,486	4,762,854
2019-2023	2,912,000	3,280,524	41,347	45,544	2,953,347	3,326,068
2024-2028	3,755,000	2,122,715	56,075	30,817	3,811,075	2,153,532
2029-2032	4,109,000	617,925	67,358	10,844	4,176,358	628,769
Unmatured	-	-	1,198,928	-	1,198,928	-
TOTAL	\$ 22,325,000	\$ 17,147,099	\$ 4,395,111	\$ 243,763	\$ 26,720,111	\$ 17,390,862

recorded at June 30. However, if advances exceed the amount actually collected, a borrowing from MRCC is recorded at June 30. The difference between the advances and the final settlement from MRCC for the fiscal year 2008 resulted in a receivable of \$383,353.

As per Ordinance Number 28, Series 2005-2006, enacted on February 6, 2006, the new tax rates per annum are 10.43% for real property and 8.43% for personal property for which 1.03% of both belong to the Commonwealth of Puerto Rico and 9.40% and 7.40%, respectively, belongs to the **Municipality**. From the portion belonging to the **Municipality**, 6.00% and 4.00%, respectively, represents the **Municipality's** basic tax rate that is appropriated for general purposes and therefore accounted for though

NOTE 11 DEBT RETIREMENT

the general fund.

Revenues of the debt service fund consists 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** (See Note 12).

The remaining portion belonging to the **Municipality** of 3.40% represents the ad-valorem property taxes withheld by the Municipal Revenue Collection Center of the Commonwealth of Puerto Rico and restricted for debt service, which is accounted for through the debt service fund (See Note 11). The **Municipality** has reached the maximum statutory tax rate limit for the basic tax while there is no limitation for the ad-valorem tax rate.

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.

The Commonwealth of Puerto Rico grants complete real property tax exoneration on the first \$15,000 has assessed valuation on residential units occupied by their owners. However, the **Municipality** receives the full amount levied, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. The Municipal Revenue Collection Center, instead of the property taxpayer, becomes the source of payment in these cases.

NOTE 12 PROPERTY TAXES

The MRCC is responsible for the assessment of all real and personal property located within the **Municipality** and for the levy, administration and collection of the corresponding tax contribution.

The **Municipality** grants a complete exemption from personal property taxes up to an assessment value of \$50,000, to retailers with an annual net sales volume of less than \$150,000. The Municipal Revenue Collection Center advances to the **Municipality**, on monthly payments, 100% of the contribution assessed over property for each fiscal year. In accordance to Law, these advances will be contributions by the Municipal Revenue Collection Center from taxpayers. The Municipal Revenue Collection Center periodically informs to the **Municipality** the amounts collected from taxpayers and applied to outstanding advances.

The personal property tax is self assessed by the taxpayer on a return, which is to be filed and paid in full by May 15 of each year with the MRCC and based on current values as of December 31 of previous year. Real property tax is assessed by the MRCC on each piece of real estate and on each building or residence. The property tax contribution is levied each year over the appraised value of the real property at the beginning of the calendar year. The real property assessment is based on the current value existing in the year 1957.

The **Municipality** records as revenue in the general fund the property tax contribution when received from monthly advances from Municipal Revenue Collection Center.

The MRCC is responsible for the billing of real property taxes and collections of both, personal and real property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the MRCC informs the **Municipality** of the estimated amount of property taxes expected to be collected for the ensuing fiscal year. Throughout the year, the MRCC advances funds to the **Municipality** based on the initial estimated collections. The MRCC 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

Due to the fact that collections of property tax are applied to the advances of property tax paid by the Municipal Revenue Collection Center, the amortization of the advance at end of year was not available due to that is in process of verification by external auditors.

continue

NOTE 13 VOLUME OF BUSINESS TAX

Volume of Business Tax is recorded in the fiscal year in which payments are due and, accordingly, represents taxes which are due and uncollected at June 30, 2008. The Volume of Business Tax is determined based on the gross income of all commerce and industrial organizations that have operations in the **Municipality**, and are not totally or partially exempt under the Industrial Incentive Law of Puerto Rico.

An annual return of business volume should be filed on or before April 15 of each year and payable in two equal installments due on July 1 and January 1. A discount of 5% is allowed when full payment is made on or before April 15. The rates of municipal license in the **Municipality** are as follows:

- a. 1.50% for financial institutions and savings and loan associations.
- b. 0.40% for all other organizations.

Taxes are payable in two equal semi-annual installments on July 1 and January 1 following the date of levy. If they are paid with declaration, the taxpayer is granted a 5% of discount. Collections of taxes during current fiscal year, applicable to the next fiscal year, are recorded as deferred revenues in the General Fund.

NOTE 14 SALES TAXES

Municipality has established a Sales and Use Taxes of 1.5% (1% to the **Municipality** and .5% to the PR Department of Treasury) effective on January 1st, 2007 on all sales of goods and properties and a variety of other transactions. This tax is to be collected by any merchant dedicated to a business which sells or provides any goods or services described as taxable by the Law or any other ruling set forth by the Municipal Legislature.

The sales tax will apply to all sales, rent contracts, or use transactions, with some exceptions as defined by the ordinance. All merchants required to collect the Sales and Use Tax, are required to file a monthly Sales and Use Tax Return Form, no later than the 20th of the following month from the month being reported.

NOTE 15 CONSTRUCTION TAX

Construction Tax is recorded in the fiscal year in which payments are due and, accordingly, represents taxes which are due and uncollected at June 30, 2008. The Construction Tax is determined based on the total amount of the construction cost of the project.

Any construction project, which doesn't qualify for any of the exceptions presented below, will pay a tax of 4% of the total cost amount of the project. The exceptions for the 4% Construction Tax imposed by the **Municipality** are as follows:

- a. 5.00% of the total cost of the project for any construction involving movement of land.
- b. 2.00% for all low income housing projects, and educational institutions of primary and secondary level.

- c. When construction is for a residence, made of at least 50% concrete, and said residence is not part of a housing project, urbanization, condominium, or any project of a similar nature; a fixed rate of \$25.00 will be collected up to a maximum total construction cost of \$50,000. In addition, for every \$1,000 in excess of the \$50,000 in total construction costs, a \$5.00 rate will be collected.

Taxes are payable before beginning construction or any activity related to the construction. Collections of taxes during current fiscal year, applicable to the next fiscal year, are recorded as deferred revenues in the General Fund.

NOTE 16 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 Special Revenue and the Capital Project Funds. Federal Financial Assistance is recorded in the Special Revenue Fund.

NOTE 17 PENSION PLAN

Employees of **Municipality** participate in the Employee's Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (ERS). The ERS is cost-sharing multiple-employer defined benefit pension plan sponsored by the Commonwealth of Puerto Rico under the Act No. 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 instrumentalities 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 Instrumentalities, Assistants to 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.

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.

NOTE 17 PENSION PLAN (continuation)

Members who have attained at least 55 years of age and have completed at least 25 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life. The amount of the annuity shall be 1.5% of the average salary, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average salary, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month. 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.

Law Number 305 was enacted on September 24, 1999, amended the Act Number 447 for the purpose of establishing a new program (System 2000). System 2000 became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999, may elect either to stay in the defined-benefit plan or transfer to the new savings program. Persons joining the government on or after January 1, 2000, will only be allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan there will be a pool of pension assets, which will be invested by the System, together with those of the current defined-benefit plan. Benefits at retirement age will not be guaranteed by the Commonwealth of Puerto Rico. The annuity will be based on a formula which assumes that each year the employees' contribution (with 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.

Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employers' contributions (9.275% of the employees' salary) will be used to fund the current plan.

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 of 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.

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:

Disability retirement benefits are available to members for occupational and non-occupational disability up to a maximum benefit of 50% of the average salary, as defined. However, for non-

occupational disability, a member must have at least 10 years of creditable service.

The **Municipality** follows the provisions of GASB Statement No. 27, *Accounting for Pensions Pension by State and Local Governmental Employers*, which requires employers that participate in cost-sharing multi-employer defined-benefits plans to recognize pension expenditures/expense equal to the employer's contractually required contributions and a liability for unpaid contributions.

The total pension expenditures/expenses recorded in the category of administration for the Fiscal Year Ended June 30, 2005 through 2008 was as follow:

FISCAL YEAR	LAW NO. 447	SYSTEM 2000
2008	\$ 253,525	\$ 171,756
2007	277,587	172,628
2006	298,369	172,374
2005	304,338	151,422
2004	312,270	104,035

The Employee's Retirement System of the Commonwealth of Puerto Rico provides additional information of the ERS. They issue a publicly 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, PR 00940-2003.

NOTE 18 SOLID WASTE LANDFILL CLOSING AND POSTCLOSING COSTS

State and Federal laws and regulations require the **Municipality** to place a final cover on its landfill when closed and perform certain maintenance and monitoring function at the landfill site for thirty years after closure. In addition to the operating expenditures related to current activities of the landfill, an expense provision and related liability are being recognized based on futures closure and post-closure care costs that will be incurred near or after the date the landfill no longer accepts waste. The **Municipality** has performed a study of the activities that need to be implemented at the **Municipality's** landfill to comply with applicable laws and regulations. As result of this study, the **Municipality** has decided to privatize the solid waste disposal service. The **Municipality** is entitled, under the agreement, to certain revenues resulting from the use of the landfill. As part of the agreement the contractor will assume the closure and post-closure costs during the next thirty years, releasing the **Municipality** of the estimated liability for future closure and post-closure care costs.

YEARS OF SERVICE	PARTICIPANT'S AGE	PENSION BENEFITS
30 or more	55 or more	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).

continue

NOTE 19 CONTINGENCIES

A. Claims and Judgments

The **Municipality** is, at present, a defendant in a number of legal matters that arise from alleged improper application of policies and negligence in the ordinary course of the **Municipality's** activities. The legal counsel of the **Municipality** has advised that at this stage in the proceedings of lawsuits he cannot offer an opinion as to the probable outcome.

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 counsel with the information currently available can not determine the final outcome of these claims, with the exception of three (3) lawsuits related to forceful expropriation, to which the legal counsel has estimate a potential loss of \$101,227. Accordingly, the financial statements include this provision in the Long-Term Liabilities.

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 Commitments

The **Municipality** had commitments of approximately of \$1.5 million for the construction, improvements, or renovation of several facilities.

END OF NOTES

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO

REQUIRED SUPPLEMENTARY INFORMATION
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
For the Fiscal Year Ended June 30, 2008

	Budget Amounts		Actual Amounts	Variance with
	Original	Final	(Budgetary Basis) (See Note A)	Final Budget
BUDGETARY FUND BALANCE, JULY 1, 2007	\$ 4,065,604	\$ 4,065,604	\$ 4,065,604	\$ -
Resources (Inflows):				
Property Taxes	8,305,769	8,305,769	8,305,942	173
Volume of Business Taxes	4,648,365	4,648,365	5,639,390	991,025
Intergovernmental Revenues	3,304,981	3,304,981	3,676,787	371,806
License and Permits	1,816,500	1,816,500	962,627	(853,873)
Interests	1,310,000	1,310,000	1,702,198	392,198
Miscellaneous	838,700	838,700	1,646,878	808,178
Total Resources (Inflows)	20,224,315	20,224,315	21,933,822	1,709,507
Amounts Available for Appropriation	24,289,919	24,289,919	25,999,426	1,709,507
Charges to Appropriations (Outflows):				
Mayor and Municipal Legislature	2,944,875	2,993,876	2,969,210	24,666
General Government	6,518,860	7,021,653	6,064,934	956,719
Public Safety	1,288,591	1,389,224	833,510	555,714
Public Works	3,442,640	3,377,896	2,576,049	801,847
Culture and Recreation	1,577,530	1,618,577	1,338,793	279,784
Health and Sanitation	1,879,553	1,912,659	1,690,611	222,048
Human Services and Welfare	1,900,305	1,895,437	1,318,790	576,647
Urban Development	30,000	30,000	26,713	3,287
Capital Outlays	114,500	241,145	183,054	58,091
Transfer to Other Funds	527,461	787,461	787,461	-
Total Charges to Appropriations	20,224,315	21,267,928	17,789,125	3,478,803
BUDGETARY FUND BALANCE, JUNE 30, 2008	\$ 4,065,604	\$ 3,021,991	\$ 8,210,301	\$ 5,188,310

See accompanying Notes to Required Supplementary Information.

NOTE A Explanation of Differences Between Budgetary Inflows and Outflows and GAAP Revenues and Expenditures

	<u>General Fund</u>
Sources/Inflows of Resources:	
Actual Amounts (Budgetary Basis) "Available for Appropriation" from the Budgetary Comparison Schedule (See Page 30)	\$ 25,999,426
Difference – Budget to GAAP:	
The Fund Balance at the Beginning of Year is a budgetary resource but is not a Current-Year Revenue for financial reporting purposes	<u>(4,065,604)</u>
Total Revenues as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 15)	<u>\$ 21,933,822</u>
Uses/Outflows of Resources:	
Actual Amounts (Budgetary Basis) "Total Charges to Appropriation" from the Budgetary Comparison Schedule (See Page 30)	\$ 17,789,125
Difference – Budget to GAAP:	
Encumbrances for supplies and equipment ordered but not received are reported in the year the order is placed for budgetary reporting purposes	(765,460)
Payments of encumbrances of prior year that are expenditures for financial reporting purposes but are not outflows for budgetary purposes	230,226
Transfers to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes	<u>(787,461)</u>
Total Expenditures as Reported on the Statement of Governmental Funds Revenues, Expenditures and Changes in Fund Balance (See Page 15)	<u>\$ 16,466,430</u>

NOTE B Explanation of Differences Between Budgetary Fund Balance and GAAP Fund Balance

Budgetary Fund Balance, June 30, 2008	\$ 8,210,301
Timing Differences:	
Change in Encumbrances	(535,234)
Cancelation of Prior Year Encumbrances	<u>(558,737)</u>
Unreserved Fund Balance, June 30, 2008	<u>\$ 7,116,330</u>

END OF THIS SECTION

PART II

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
AND REPORTS REQUIRED BY GOVERNMENT AUDITING
STANDARDS AND OMB CIRCULAR A-133**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF FAJARDO, PUERTO RICO**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Fiscal Year Ended June 30, 2008**

FEDERAL GRANTOR / PASS THROUGH GRANTOR / PROGRAM OR CLUSTER TITLE	FEDERAL CFDA NUMBER	PASS-THROUGH ENTITY IDENTIFYING NUMBER	FEDERAL EXPENDITURES
U.S. Department of Agriculture:			
USDA – Rural Development:			
Rural Housing Preservation Grants	10.433	N/AV	\$ 21,396
Pass-Through Administration of Families and Children:			
Child and Adult Care Food Program (USDA)	10.558	N/AV	<u>412,732</u>
Total U.S. Department of Agriculture.....			<u>434,128</u>
U.S. Department of Housing and Urban Development:			
Community Development Block Grant (CDBG).....	14.218	B-05-MC-720012 B-06-MC-720012 B-07-MC-720012	31,604 995,130 <u>154,946</u>
			1,181,680
Section 8 Housing Choice Voucher Program	14.871		<u>426,451</u>
Total U.S. Department of Housing and Urban Development ...			<u>1,608,131</u>
U. S. Department of Health and Human Services:			
Pass-Through Administration for the Childhood Care and Integral Development:			
Child Care and Development Block Grant.....	93.575	N/AV	29,654
Head Start Program	93.600	02-CH-9944/04 AD	<u>3,863,670</u>
Total U.S. Department of Health and Human Services.....			<u>3,893,324</u>
U.S. Department of Homeland Security:			
Pass-Through Governor Authorized Representative:			
Homeland Security Program	97.067	N/AV	<u>84,340</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$6,019,923</u>

See accompanying Notes to Schedule of Expenditures of Federal Awards.

NOTE 1 GENERAL

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activities of the **Municipality of Fajardo, Puerto Rico**. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this Schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements. The **Municipality** reporting entity is defined in Note (1) (A) to the basic financial statements. All federal financial awards received directly from federal agency as well as federal financial awards passed-through other government agencies are included on the Schedule.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- A. 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.
- B. 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.
- C. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable or when actually paid, whichever occurs first.

NOTE 3 FEDERAL CFDA NUMBER

The CFDA 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.

NOTE 4 PASS-THROUGH GRANTOR'S NUMBER

State or local government redistribution 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 subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

NOTE 5 RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Expenditures of federal awards are reported in the **Municipality's** Statement of Revenues, Expenditures and Changes in Fund Balances- Governmental Fund as follows: Head Start - \$3,863,670 and Other Governmental Funds \$2,156,293.

NOTE 6 MAJOR PROGRAMS

Major programs are identified in the Summary of Auditor's Results Section of the Schedule of Findings and Questioned Costs.

END OF NOTES



201 Gautier Benítez Ave.
Consolidated Mall C-31
PO Box 8369
Caguas, PR 00726-8369
Phones: (787) 746-0510 / 746-1185 / 746-1370
Fax: (787) 746-0525
cpdiazmartinez@hotmail.com

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY GOVERNMENT AUDITING STANDARDS

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of **Municipality of Fajardo, Puerto Rico (Municipality)**, as of and for the fiscal year ended June 30, 2008, which collectively comprise the **Municipality's** basic financial statements and has issued our report thereon dated December 18, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Entity's internal control over financial reporting.

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

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weakness. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.



Estado Libre Asociado de Puerto Rico

Gobierno Municipal de Fajardo

Oficina de Finanzas

13 de enero de 2009

A LA MANO

Sr. Omar Negrón
Comisionado
Oficina Comisionado de
Asuntos Municipales
GPO Box 70167
San Juan, PR 00936-0167

Estimado Comisionado Negrón:

Acompañamos una (1) copia de los ***“Basic Financial Statements” with Additional Reports and Information Required by the Government Auditing Standards and OMB Circular A-133 del Municipio de Fajardo***, para el Año Fiscal terminado el 30 de junio de 2008.

Gracias por su atención.

Cordialmente,

María I. Colón
Directora de Finanzas

oef
anejo

09 JAN 15 PM 1:08
RECEIVED
UNIDAD DE CORREO
P/1/09
109

COMPTON
EX-100