

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

MUNICIPIO DE GURABO
AUDITORIA 2001-02
30 DE JUNIO DE 2002

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DE ASUNTOS MUNICIPALES
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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
GENERAL PURPOSE FINANCIAL STATEMENTS
(with Independent Auditors' Report Thereon)
FISCAL YEAR ENDED
JUNE 30, 2002

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INDEPENDENT AUDITOR'S REPORT

Hon. José A. Rivera Rodríguez
Mayor
Commonwealth of Puerto Rico
Municipality of Gurabo

We have audited the accompanying general purpose financial statements of the Municipality of Gurabo, as of and for the year ended June 30, 2002, as listed in the table of contents. These general purpose financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

Except as discussed in the following paragraph, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1 the Municipality of Gurabo has not maintained complete and adequate records related to the fixed assets of the General Fixed Assets Account Group, specifically for retirements of property, plant and equipment. Accordingly, we were unable to satisfy ourselves as to the fixed assets balance or such all groups amounting to \$29,130,965.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the general fixed assets balances, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the Municipality of Gurabo as of June 30, 2002, and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

PANNELL KERR FORSTER, LLP

*Hon. José A. Rivera, Mayor
Commonwealth of Puerto Rico
Municipality of Gurabo*

In accordance with Government Auditing Standards, we have also issued under separate cover, our report dated July 3, 2003 on our consideration of the Municipality of Gurabo's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of the audit.



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July 3, 2003

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO

Combined Balance Sheet

All Fund Types and Account Groups
June 30, 2002

	Governmental Funds Types				Account Groups		Totals (Memorandum Only)
	General	Special Revenues	Debt Service	Capital Projects	General Fixed Assets	General Long-term Debt	
Assets							
Cash and investments	\$ 7,131,715	\$ 720,208	\$ -	\$ 1,051,655	\$ -	\$ -	\$ 8,903,578
Cash with fiscal agent	-	-	1,651,065				1,651,065
Accounts receivable (net of allowance for uncollectibles)							
Due from other funds	291,341	1,142,042		1,842,642	-	-	3,276,025
Due from federal agencies		443,711		281,242	-	-	724,953
Volume of business tax receivable	67,923	-	-	-	-	-	67,923
Rent Receivable	8,030	-	-	-	-	-	8,030
Land	-	-	-	-	977,200	-	977,200
Property and equipment	-	-	-	-	28,153,765	-	28,153,765
Amount available in debt service fund	-	-	-	-	-	1,491,685	1,491,685
Amount to be provided for retirement of bonds, notes and loans	-	-	-	-	-	3,088,360	3,088,360
Amount to be provided for retirement of debts with other governments	-	-	-	-	-	384,382	384,382
Amount to be provided for litigations	-	-	-	-	-	2,772,667	2,772,667
Amount to be provided for payment of accrued compensated absences	-	-	-	-	-	774,912	774,912
Total assets	\$ 7,499,009	\$ 2,305,961	\$ 1,651,065	\$ 3,175,539	\$ 29,130,965	\$ 8,512,006	\$ 52,274,545

See notes to general purpose financial statements

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO

Combined Balance Sheet

All Fund Types and Account Groups
June 30, 2002

	Governmental Fund Types				Account Groups		Totals (Memorandum Only)
	General	Special Revenue	Debt Service	Capital Projects	General Fixed Assets	General Long-term Debt	
<u>Liabilities</u>							
Accounts payable and accrued liabilities	\$ 1,325,281	\$ 51,873	\$ -	\$ 163,857	\$ -	\$ -	\$ 1,541,011
Due to other funds	2,984,684	264,229	-	27,112	-	-	3,276,025
Deferred volume of business tax revenues	3,649,030	-	-	-	-	-	3,649,030
Due to other governments	117,104	-	-	-	-	-	117,104
Deferred federal revenues	-	411,052	-	405,192	-	-	816,244
Other deferred and credits	72,281	-	-	-	-	-	72,281
Bonds and notes payable	-	-	159,380	-	-	4,580,045	4,739,425
General obligations other debts payable	-	-	-	-	-	384,382	384,382
General obligation amount for litigations	-	-	-	-	-	2,772,667	2,772,667
General accrued vacations and sickleave payable	-	-	-	-	-	774,912	774,912
Total liabilities	8,148,380	727,154	159,380	596,161	-	8,512,006	18,143,081
<u>Fund Equity</u>							
Investment in general fixed assets	-	-	-	-	29,130,965	-	29,130,965
Fund balances							
Reserved for encumbrances	1,439,035	314,223	-	-	-	-	1,753,258
Reserved for debt service	-	-	1,491,685	-	-	-	1,491,685
Reserved for capital projects	-	-	-	200,925	-	-	200,925
Unreserved	(2,088,406)	1,264,584	-	2,378,453	-	-	1,554,631
Total fund equity	(649,371)	1,578,807	1,491,685	2,579,378	29,130,965	-	34,131,464
Commitments and contingencies (notes 8, 9 and 10)	-	-	-	-	-	-	-
Total liabilities and fund equity	\$ 7,499,009	\$ 2,305,961	\$ 1,651,065	\$ 3,175,539	\$ 29,130,965	\$ 8,512,006	\$ 52,274,545

See notes to general purpose financial statements

MUNICIPALITY OF GURABO

Combined Statement of Revenues, Expenditures and Changes in Fund Balances

All Governmental Fund Types
Year Ended June 30, 2002

	Governmental Funds Types				Totals (Memorandum Only)
	General	Special Revenue	Debt Service	Capital Projects	
Revenues:					
Property taxes	\$ 5,626,946	\$ -	\$ 1,159,242	\$ -	\$ 6,786,188
Municipal license tax	2,549,174	-	-	-	2,549,174
Licenses and permits	1,177,261	-	-	-	1,177,261
Federal grants and contributions	-	1,434,117	-	341,044	1,775,161
Fines and penalties	2,105	-	-	-	2,105
Interest	82,586	977	23,960	40,441	147,964
Intergovernmental	933,455	1,107,045	-	430,500	2,471,000
Miscellaneous	182,704	-	-	-	182,704
Total revenues	<u>10,554,231</u>	<u>2,542,139</u>	<u>1,183,202</u>	<u>811,985</u>	<u>15,091,557</u>
Expenditures					
Current:					
General government	4,312,383	503,104	-	-	4,815,487
Public safety	815,963	366,251	-	-	1,182,214
Public works	2,667,117	10,997	-	-	2,678,114
Culture and recreation	667,178	-	-	-	667,178
Health and Welfare	245,835	1,694,588	-	-	1,940,423
Capital outlays	306,098	54,481	-	511,469	872,048
Debt service:					
Principal	-	-	389,244	-	389,244
Interest	-	-	369,912	-	369,912
Total expenditures	<u>9,014,574</u>	<u>2,629,421</u>	<u>759,156</u>	<u>511,469</u>	<u>12,914,620</u>
Excess (deficiency) of revenues over expenditures	1,539,657	(87,282)	424,046	300,516	2,176,937
Other financing sources (uses) (Notes 1,2,5 and 7)					
Proceeds debt refinancing	665,000	-	-	-	665,000
Operating transfer in	28,477	407,000	76,289	330,066	841,832
Operating transfer out	(813,355)	-	(28,477)	-	(841,832)
	<u>(119,878)</u>	<u>407,000</u>	<u>47,812</u>	<u>330,066</u>	<u>665,000</u>
Excess of revenues and other financing sources over expenditures and other financing uses	<u>1,419,779</u>	<u>319,718</u>	<u>471,858</u>	<u>630,582</u>	<u>2,841,937</u>
Fund balances at beginning of year (as previously reported)	(2,069,150)	1,584,129	1,019,827	1,004,606	1,539,412
Prior period adjustment	-	(325,040)	-	944,190	619,150
Fund balances at beginning of year (as restated)	<u>(2,069,150)</u>	<u>1,259,089</u>	<u>1,019,827</u>	<u>1,948,796</u>	<u>2,158,562</u>
Fund balances at end of year	\$ <u>(649,371)</u>	\$ <u>1,578,807</u>	\$ <u>1,491,685</u>	\$ <u>2,579,378</u>	\$ <u>5,000,499</u>

MUNICIPALITY OF GURABO

Statement of Revenues and Expenditures
 Budget and Actual- General Fund
 Non GAAP Budgetary Basis
 For the Year Ended June 30, 2002

	<u>Budget</u>	<u>Actual</u>	<u>Variance Favorable (Unfavorable)</u>
Revenues:			
Property taxes	\$ 5,056,767	\$ 5,626,946	\$ 570,179
Municipal license taxes	2,705,000	2,549,175	(155,825)
Licenses and permits	850,000	1,177,261	327,261
Fines and penalties	3,000	2,105	(895)
Interest	70,000	82,586	12,586
Intergovernmental	969,048	933,455	(35,593)
Operating transfer-in	-	28,477	28,477
Proceeds from debt refinancing	-	665,000	665,000
Miscellaneous	33,083	182,740	149,657
City Council Resolutions	<u>1,699,358</u>	<u>1,699,358</u>	<u>-</u>
Total revenues	<u>11,386,256</u>	<u>12,947,103</u>	<u>1,560,847</u>
Expenditures:			
General government	5,997,374	4,855,666	1,141,708
Public safety	977,339	913,178	64,161
Public works	3,343,993	2,975,914	368,079
Culture and recreation	727,543	686,304	41,239
Health and welfare	254,007	246,680	7,327
Operating transfer out	<u>86,000.00</u>	<u>813,355</u>	<u>(727,355)</u>
Total expenditures	<u>11,386,256</u>	<u>10,491,097</u>	<u>895,159</u>
Excess of revenues over expenditures	<u>\$ -</u>	<u>\$ 2,456,006</u>	<u>\$ 2,456,006</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS
JUNE 30, 2002

Note 1 - Organization and summary of significant accounting policies

The Municipality of Gurabo (the Municipality), founded in 1815, is a municipality of the Commonwealth of Puerto Rico. It is governed by a Mayor and a 14 member Municipal Assembly elected for a four-year term. The Municipality provides services to its residents in the areas of health, welfare, public works, education, public safety, public housing, community development, culture and recreation, and other services.

The accompanying general purpose financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as applicable to governmental entities. The following is a summary of significant accounting policies:

A. Financial reporting entity

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14 of the Governmental Accounting Standards Board (GASB). The basic, but not the only criterion for including a potential component unit within the reporting entity, is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary government appoints a voting majority of the entity's governing body and if either one of the following conditions exist; the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. Based on the above criteria there are no potential component units, which should be included in the general purpose financial statements.

B. Measurement focus, basis of accounting, and basis of presentation

The accounts of the Municipality are organized and operate on the basis of funds and account groups. A fund is an independent fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The minimum number of funds is maintained consistent with legal and managerial requirements. Account groups are a reporting device to account for certain assets and liabilities of the governmental funds not recorded directly in those funds. The various funds are summarized by type in the accompanying general-purpose financial statements. The Municipality records its transactions in the fund types and account groups described below. Transactions between funds within a fund type, if any, have been eliminated.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Governmental fund types

Governmental funds are used to account for the Municipality's expendable financial resources and the related liabilities. The measurement focus is upon determination of any changes in financial position. Governmental funds are comprised of:

General fund

The general fund is used to account for all financial transactions, except those required to be accounted for in another fund.

Special revenue fund

Special revenue fund is used to account for the proceeds of specific revenue sources (other than debt service or capital projects) such as federal grants, that are legally restricted to expenditures for specified purposes.

Debt service fund

The debt service fund is used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest and related costs.

Capital projects fund

Capital projects fund is used to account for financial resources to be used for the acquisition or construction of major capital facilities, other than those financed by proprietary funds.

Account groups

Account groups are used to establish accounting control and accountability for the Municipality's general fixed assets and the unmatured principal of its general long-term debt and other long-term obligations.

General fixed assets account group

This account group is used to account for all general fixed assets of the Municipality, other than those accounted for in the enterprise fund.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

General long-term debt account group

This account group is used to account for all long-term debt including bonds, notes, loans and other long-term liabilities, other than those accounted for in the enterprise fund.

C. Basis of accounting

The basis of accounting determines when the Municipality recognizes revenues and expenditures and related assets and liabilities.

Governmental fund types follow the modified accrual basis of accounting. Under this basis of accounting, revenues are recorded in the accounting period in which they become susceptible to accrual, that is, when they become both measurable and available. Available is defined as expected to be collected within the current period or soon enough thereafter to be used to pay liabilities of the current period.

In applying the susceptible to accrual concept to governmental revenues, there are essentially two types of revenues. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the Municipality; therefore, revenues are recognized based upon the expenditures incurred. In the other, monies are virtually unrestricted and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenues at the time of receipt or earlier if the susceptible to accrual criteria are met.

The Municipality reports deferred revenue on its combined balance sheet. Deferred revenue arises when potential revenue does not meet both the measurable and available criteria for recognition in the current period. Deferred revenue also arises when the Municipality receives resources before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures.

In subsequent periods, when both revenue recognition criteria are met, or when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed from the combined balance sheet and revenue is recognized.

Expenditures and related liabilities are generally recorded, except as described below, in the accounting period in which the liability is incurred. Expenditures and related liabilities for interest on long-term obligations, are recorded when due, except for interest due July 1st of the following year which is accounted for as paid on June 30. Vacation, sick leave, disallowances and litigation are recorded in the general long-term debt account group.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Licenses, permits, service charges, fines and forfeits, investment income and miscellaneous revenues are recorded as revenues on the cash basis, which includes amounts collected shortly after June 30.

D. Budgetary accounting

The Municipality's annual budget is prepared on the budgetary basis of accounting and represents departmental appropriations recommended by the Mayor and approved by the Municipality's City Council prior to the beginning of the fiscal year. Budgetary control is maintained at the department level for each individual appropriation.

Amendments to the budget, and budgetary transfers related to personal expenditures, require the approval of the Municipality's City Council.

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 Statement of Revenues and Expenditures - Budget and Actual - General Fund is presented on the budgetary basis to enhance comparability.

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

1. Encumbrances are considered as expenditures for budgetary purposes.
2. Prior year encumbrances settled during the year and recorded as expenditures for GAAP basis.
3. Effect of GAAP basis accruals.
4. Effect of Municipality's City Council resolutions less any deferred revenue recognized as revenue during the year.

The following is reconciliation, of the differences between GAAP and the budgetary basis for the general funds excess of expenditures and other financing uses over revenues and other financing sources:

GAAP basis	\$ 1,419,779
Prior year encumbrances settled during the current year	775,904
Current year encumbrances treated as current year expenditures for budgetary purposes	(1,439,035)
Budgetary readjustments approved by the Municipal Assembly	<u>1,699,358</u>
	<u>\$ 2,456,006</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

E. Cash, cash equivalents, and investments

Substantially all cash balances are commingled in a general checking account, certificates of deposit and several special purpose bank accounts, except for cash and investments restricted by law. Each fund records its equity interest in the pooled cash balance. The available cash balance in the general checking account beyond immediate needs is invested in interest-bearing deposits. Investment earnings are all credited to the general fund.

Cash with fiscal agent represents property tax collections retained by the "Centro de Recaudaciones de Ingresos Municipales" (CRIM) and restricted for the payment of the Municipality's debt service.

F. Interfund transactions

The Municipality has the following types of transactions among funds:

Operating transfers - Transfers that are reported when incurred as "Operating transfers in" by the recipient fund and as "Operating transfers out" by the disbursing fund. Transfers from the general fund to the enterprise fund to subsidize operations are recorded as operating transfers.

Receivables and payable - Transactions between funds outstanding at the end of the fiscal year are referred as due to/from other funds. The general fund provides services, at cost, to other funds. The amounts charged to other funds are treated as reductions in expenditures of the general fund.

G. General fixed assets

General fixed assets acquired or constructed are reported as expenditures in the fund that finances the acquisition and are capitalized at cost in the general fixed assets account group. Donated general fixed assets are reported at estimated fair market value at the date received.

Certain improvements such as roads, streets, bridges, curbs and gutters sidewalks are not capitalized. Such assets normally are immovable and of value only to the Municipality. Therefore, the purpose of stewardship for capital expenditures is satisfied without recording these assets. Depreciation is not recorded in the general-fixed assets account group.

The Municipality does not maintain adequate records for its fixed assets and management was not able to make an assertion as to the completeness of the General Fixed Assets Group of Accounts. However, at present the Finance Department is in the process of updating these records and performing a physical inventory of equipments in order to maintain a proper system in the future.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

H. Compensated absences

Employees accrue vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. This liability is presented in the general long-term debt account group because it will not be funded with available expendable financial resources at June 30, 2002.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated unpaid sick leave at the then current rate, if the employee has at least 10 years of service with the Municipality. This liability is presented in the general long-term debt account group because it will not be funded with available expendable financial resources at June 30, 2002.

General long-term debt for compensated amounts to \$774,912 includes \$334,873 of accrued vacation benefits and \$440,039 of accrued sick leave benefits, representing the Municipality's commitment to fund such compensated absences from future operations.

I. Long-term debt

The liabilities reported in the general long-term debt account group include the Municipality's general obligation bonds and notes, and other long-term liabilities including vacation, sick leave, and litigation.

J. Reserves of fund balance

Reserves of fund balance represent portions of fund balances that are legally segregated for a specific future use or are not appropriable for expenditure. The Municipality has the following reservations of fund balance:

Encumbrances represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

Debt service - Represents net assets available to finance future debt service payments.

Capital projects - Represent net assets available to finance future capital outlays.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

K. Claims and judgments

The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund. The general long-term debt account group 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.

L. Total (memorandum only) columns

Total columns on the general-purpose financial statements are captioned as "memorandum only" because they do not represent consolidated financial information and are presented only to facilitate analysis. The columns do not present information that reflects financial position, results of operations, or cash flows in accordance with generally accepted accounting principles. Interfund eliminations have not been made in the aggregation of these data.

Note 2 - Annual revenues

A. Property taxes

The Municipal Revenue Collection Center (the Center) was created by Law No. 80 as part of the Municipal Reform Act of August 30, 1991. The Center was created for the purpose of establishing a separate and independent governmental entity from the Commonwealth of Puerto Rico (the Commonwealth), to bill, collect, receive and distribute the property tax revenues of the Municipalities. Prior to the enactment of this law, the Commonwealth, through the Department of the Treasury, accounted for these revenues.

Pursuant to Law No. 80, the Center is empowered to bill and collect property taxes and distribute property tax collections to the Municipality.

The Center must advance to the Municipality, on a monthly basis, one twelfth of the estimate of annual revenue for the Municipality. A final liquidation of funds due from or to the Municipality by the Center is required within six and twelve months, following the close of the fiscal year on June 30, respectively. The amount receivable or payable arising from the fiscal year end liquidation is not known at June 30, 2002.

Real and personal property are assessed based on the taxable values as of January 1, for all properties located in the Municipality. Assessed values of real property are established at current values in 1957. Assessed values of personal property are based on the book value at January 1 of each year. Real property taxes are billed by the Center and are due in two equal installments in July and January following the assessment date. Personal property taxes are self assessed and are due on May 15, when the related property tax return is required to be filed.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Complete real property tax exoneration is granted by the Commonwealth of Puerto Rico on the first \$15,000 of the assessed valuation of owner occupied residential units. 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. Complete exemption from personal property taxes up to an assessment of \$50,000 is granted to retailers with an annual volume of net sales under \$150,000. The Department of the Treasury instead of the property taxpayer becomes the source of payment in these cases.

The annual tax rate for fiscal year 2002 is 7.83% for real property and 5.83% for personal property. The annual tax rate is comprised of a basic minimum tax of 4% for personal property and 6% for real property which is appropriated for general purposes and accounted in the general fund; 1.03% assessed by the Commonwealth of Puerto Rico for the payment of general obligation bonds and an amount assessed by the municipality for the payment of municipal bonds and notes.

Several Commonwealth of Puerto Rico Laws, primarily to promote economic development, provide Property tax exemptions. Under various industrial incentive laws, qualifying businesses are exempted totally or partially from real and personal property taxes. Retailers with annual sales volume of less than \$150,000 are granted an exemption from taxes on the first \$50,000 of personal property.

The Commonwealth also exempts homeowners of taxes on the first \$15,000 of the assessed value of real property used by the owner as his principal residence. Veterans have an additional exemption of taxes on \$5,000 of the assessed value of real property.

Law 16 of May 1960 authorizes the Secretary of the Treasury of the Commonwealth to grant a discount of .20% of the annual basic tax over the assessment value of all real and personal property not exempt from taxes. The Department of the Treasury reimburses the discount to the Municipality.

Since the collection of property taxes from the taxpayers is under the administration of the CRIM, the Municipality records the revenues related to property taxes, net of the operational expenses allocated by the CRIM to the Municipality, when such revenues are reported by the CRIM. During the fiscal year 2002 the allocated expenses amounted to \$123,393.

The amount receivable or payable arising from the fiscal year end settlement of actual property tax collections versus property tax advances made by the CRIM to the Municipality is not known. Advances of property tax on (a) and (b) above, are recorded as revenues on the General Fund and Debt Service Fund, respectively. These amounts are preliminary and could be subject to changes. Changes will be recorded in the period reported by the CRIM.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

B. Municipal license taxes

The Municipality imposes a volume of business tax pursuant to Act No. 82 of August 30, 1991, on all business entities, which operate within the Municipality, which are not exempt from the tax pursuant to the Industrial Incentives Act. The tax is based on gross revenues, as defined by law, computed at the rate of 1.50% for financial institutions and savings and loans associations, and .50% for all other business entities.

The minimum gross revenue to file the Volume of Business Tax Declaration is \$5,000 and the minimum tax payable is \$25. The date to file the Volume of Business Tax Declaration is April 15. The Municipality grants a five percent discount, if the taxes are paid on or before April 15. Otherwise, 50% of taxes payable must be paid within the first 15 days of each semester beginning with the first semester ending December 31.

The Municipality recognized an account receivable for the estimated municipal license taxes to be collected during next year but corresponding to current year and prior years. Principal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

Note 3 - Cash, cash equivalents, and investments

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. During the year, the Municipality invested its funds in interest bearing bank accounts, and certificates of deposit.

There are three categories of credit risk that apply to the Municipality's cash and investments:

1. Insured or collateralized with securities held by the Municipality's or by the Municipality's agent in the Municipality's name.
2. Collateralized with securities held by the pledging financial institution's trust department or the Municipality's agent in the Municipality's name.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

3. Uncollateralized.

Balances held in each category are as follows:

	1	Categories 2	3	Bank Balance	Carrying Amount
Cash	\$ 3,469,636	\$ -	\$ 48,342	\$ 3,517,978	\$2,503,153
Certificates of Deposits	-	6,400,425	-	6,400,425	6,400,425
	<u>\$ 3,469,636</u>	<u>\$ 6,400,425</u>	<u>\$ 48,342</u>	<u>\$9,918,403</u>	<u>\$ 8,903,578</u>

Deposits at the Government Development Bank for Puerto Rico are restricted principally for debt service and capital projects. These are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks. Therefore these have been categorized as "Uncollateralized" in the above table.

Note 4 - Interfund transactions

Due from/to other funds

Interfund receivables and payables generally reflect temporary loans, billings for services provided and recovery of expenditures.

Following is a summary of interfund assets and liabilities as of June 30, 2002:

Receivable Fund	Payable Fund	Amount
General	Special Revenue	\$ 264,229
	Capital Project	27,112
Special Revenue	General	1,142,042
Capital Project	General	<u>1,842,642</u>
		<u>\$3,276,025</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Note 5 - Intergovernmental revenues

Sources of intergovernmental revenues are primarily of governmental payments from the Commonwealth of Puerto Rico and "in lieu of tax" payments from certain quasi public corporations, such as Puerto Rico Electric Power Authority. For the year 2001-2002 the contribution in lieu of taxes was \$838,769.

Grants and subsidies received from the Commonwealth of Puerto Rico include, among other, a general subsidy for capital improvements.

Note 6 - General fixed assets

A summary of the general fixed assets account group follows:

	Balance June 30, 2001	Additions	Retirements	Transfers	Balance June 30, 2002
Land	\$ 977,200	\$ -	\$ -	\$ -	\$ 977,200
Buildings	5,714,759	-	-	82,350	5,797,109
Equipment and vehicles	12,156,510	187,137	32,940	-	12,310,707
Construction in progress	3,556,766	684,911	-	(163,886)	4,077,791
Improvements	5,886,622	-	-	81,536	5,968,158
	<u>\$ 28,291,857</u>	<u>\$ 872,048</u>	<u>\$ 32,940</u>	<u>\$ -</u>	<u>\$ 29,130,965</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Note 7 - General long-term debt

Changes in general long-term debt for the year ended June 30, 2002 are summarized as follows:

	Bonds	Federal Loan and Notes	Loans	Total
Balance at June 30, 2001	\$ 3,856,000	\$ 695,333	\$ 500,000	\$ 5,051,333
Payments	(350,000)	(26,288)	(50,000)	(426,288)
New debt issued	665,000	-	-	665,000
Adjustments from refinancing	(710,000)	-	-	(710,000)
Balance at June 30, 2002	<u>\$ 3,461,000</u>	<u>\$ 669,045</u>	<u>\$ 450,000</u>	<u>\$ 4,580,045</u>

As of June 30, 2002, debt service requirements for the above general long-term debt, are as follows:

Fiscal Year Ending June 30	Principal	Interest	Total
2003	\$ 371,000	\$ 206,777	\$ 577,777
2004	328,000	206,079	534,079
2005	370,000	194,505	564,505
2006	299,000	176,143	475,143
2007	252,000	162,045	414,045
Thereafter	2,960,045	1,093,508	4,053,553
	<u>\$4,580,045</u>	<u>\$2,039,057</u>	<u>\$6,619,102</u>

The legal debt margin of the Municipality is equal to 10% of the total assessment of property located within the Municipality. Total property assessments, based on information reported by the Municipal Revenue Collection Center amounted to approximately \$114,685,000.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

A. Bonds

General obligation bonds payable as of June 30, 2002 are as follows:

Series	Interest Rate	Payable Through	Original Issue	Balance June 30, 2002
1982	5.00	2007	\$ 397,000	\$ 125,000
1987	8.20	2002	515,000	35,000
1987	8.20	2002	1,030,000	-
1990	6.00	2015	1,967,000	1,480,000
1991	5.00	2015	615,000	428,000
1995	5.00	2020	325,000	283,000
1999	4.75	2005	449,250	240,000
2000	7.80	2005	245,000	205,000
2002	2.7 to 5.6	2026	665,000	665,000
				\$3,461,000

B Federal loans and notes

\$704,000 note payable in annual installments of \$17,000 to \$27,000 until October 2012, interest at 4.5%.

\$ 669,045

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

C. Loans

Operational loan of \$1,000,000 payable in annual installments of \$50,000 until 2006 July 1, 2010, interest at 8% \$ 450,000

Total general obligation bonds, special and federal notes \$ 4,580,045

D. Other Long-term debt with governmental agencies

\$114,172 due to the Municipal Revenue Collection Center for property taxes advance, payable in monthly installments of \$1,903 until June 30, 2004 \$ 79,286

\$230,927 due to the Municipal Revenue Collection Center for property taxes advance, payable in monthly installments of \$3,849 until June 30, 2005 230,937

\$101,983 due to the Treasury Department, payable in monthly installments of \$773 until June 30, 2010 74,159

Total debt with other governmental agencies \$384,382

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Note 8 - Retirement System

The Municipality participates in the Employee's Retirement System of the Government of Puerto Rico and its instrumentalities (ERS), a multiple-employer contributory retirement plan, which covers only eligible full-time employees. The system provides retirement, death, and disability benefits and annuities to Commonwealth employees not covered by their own systems.

Commonwealth legislation required employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participants' gross salary. Total employee and employer contributions during the year ended June 30, 2002 amounted to approximately \$159,215 and \$182,000, respectively.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1991, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employees participating in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining on or after January 1, 2000 will only be allowed to become members of the System 2000. System 2000 will reduce the retirement age from 65 to 60 for those employees who joined the current plan on or after April 1, 1990.

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

For the year ended June 30, 2002, total payroll for all covered employees was approximately \$2,220,500. Covered payroll refers to all compensation paid by the Municipality to active employees covered by the ERS on which contributions to the pension are based.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

The amount of the annuity shall be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation multiplied by the number of years of creditable service in excess of twenty years, for those employees covered after March 31, 1990, the annuity shall be equal to one and one-half percent of the average compensation multiplied by the number of years of creditable service, in no case shall the annuity be less than \$2,400.

Note 9 - Commitments

A. Operating leases

The Municipality leases various properties and equipment under operating lease agreements, which generally have terms of one year or less and are automatically renewed if sufficient funds are available. Lease agreements covering periods in excess of one-year are cancelable at the Municipality's option upon 30 days written notice to the lessor. Rental expenditures for the year ended June 30, 2002 amounted to approximately \$48,500.

B. General commitments

The Municipality has commitments to invest approximately \$4,600,000 to complete construction projects at several locations within the Municipality. Federal funds are expected to be used to satisfy all of these construction and improvement commitments.

Note 10 - Contingencies

A. Litigation

The Municipality is a defendant in legal matters that arise in the ordinary course of the Municipality's activities. With respect to pending and threatened litigation, the Municipality has reported liabilities of \$2,772,667 in the general long-term debt account group for anticipated unfavorable judgments.

The amount presented in the general long-term debt group of account represents the amount estimated as probable liability, which will require future available financial resources for its payment. The Municipality's administration and legal counsel believes that the ultimate liability in excess of amounts provided would not be significant.

In addition, the Municipality is a defendant or co-defendant in several legal proceedings, which are in the discovery stage. Certain of these claims are covered by insurance. Legal counsel with the information currently available cannot determine the final outcome of these claims. As a result, the accompanying general-purpose financial statements do not include adjustments, if any, that could result from the resolution of these legal proceedings.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

B. Federal financial assistance

The Municipality receives financial assistance from the federal government in the form of grants or entitlements. All grants are subject to financial and compliance audits by the grantor agencies, which could result in requests for reimbursement by the grantor agencies for expenditures, which are disallowed under the terms of the grants.

Note 11 – Healthcare costs

During the year ended June 30, 2000 the Governor of the Commonwealth of Puerto Rico required from the municipalities of Puerto Rico an annual contribution to subsidy the cost of the implementation and administration of the Healthcare Reform. Such contributions are required to be disbursed from general fund operating budget. Total contributions made by the Municipality amounted to approximately \$424,800 and \$363,300 for the fiscal year ended June 30, 2002.

Note 12 – GASB-34

In June 1999, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 34 (Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments). GASB-34 will significantly change the way in which the Municipality reports its finances.

GASB-34 established two bases for reporting financial information: government-wide financial statements and fund presentation. The government-wide financial statements method adopts the flow of economic resources measurement focus and accrual basis of accounting for both governmental activities and business-type activities. The basis for preparing fund financial statements is similar to conventional governmental financial statements except the focus for presentation is on major funds rather than fund types. Capital assets, including infrastructure assets, and depreciation charges are reported on the entity-wide perspective financial statements. The management’s discussion and analysis information precedes the basis financial statements but is considered required supplementary information. Budgetary information is no longer presented in the financial statements but rather is presented as required supplementary information.

GASB-34 will begin to take effect for the Municipality in fiscal year beginning after June 15, 2003.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
NOTES TO THE GENERAL PURPOSE FINANCIAL STATEMENTS (continued)
JUNE 30, 2002

Note 13 – Prior period adjustments

The Municipality restated the beginning fund balances to record the net amounts due from Federal agencies and related deferred revenues by \$619,150.

This amount is comprised of an overstatement of \$325,040 in the receivables arising for the Community Oriented Policing Services, Child Care Food, Housing Preservation and Local Law Enforcement Programs; and understatement of \$944,190 arising by receivables for the State Block Grant Program.

Note 14 – Subsequent event

During the fiscal year ended June 30, 2003 the Municipality obtained from the Government Development Bank for Puerto Rico, the issuance of \$2,715,000 general obligation bonds to be used as an operational reserve to pay in full a lawsuit that is in appeal process in the Boston Circuit of the U.S. Federal Court.

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GURABO
SINGLE AUDIT PACKAGE

Fiscal Year Ended
June 30, 2002

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

Hon. José A. Rivera Rodríguez
Mayor
Commonwealth of Puerto Rico
Municipality of Gurabo

We have audited the financial statements of the Municipality of Gurabo as of and for the year ended June 30, 2002 and have issued a qualified report thereon dated July 3, 2003. Except for the balance of general fixed assets, 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 of America.

Compliance

As part of obtaining reasonable assurance about whether the Municipality of Gurabo's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of material noncompliance that are required to be reported under *Government Auditing Standards*.

Internal control over financial reporting

In planning and performing our audit, we considered the Municipality of Gurabo's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions.

Hon. José A. Rivera Rodríguez
Mayor
Commonwealth of Puerto Rico
Municipality of Gurabo
Page 2

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Municipality of Gurabo's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as findings 2002-1 through 2002-7.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider findings 2002-1 to 2002-7 to be material weaknesses.

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



July 3, 2003

Pannon Koan Forster

License No. 22

Expires on December 1, 2004

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

Hon. José A. Rivera Rodríguez
Mayor
Commonwealth of Puerto Rico
Municipality of Gurabo

Compliance

We have audited the compliance of the Municipality of Gurabo with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2002. The Municipality of Gurabo's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Municipality of Gurabo's management. Our responsibility is to express an opinion on the Municipality of Gurabo's compliance based on our audit.

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

Hon. José A. Rivera Rodríguez
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Commonwealth of Puerto Rico
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Page 2

We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Municipality of Gurabo's compliance with those requirements.

As described in item 2002-8 in the accompanying schedule of findings and questioned costs, the Municipality did not comply with requirements regarding equipment and real property management that is applicable to its State Block Grant, Section 8 Rental for Low and Very Low Income Families Federal programs. Compliance with such requirements is necessary, in our opinion, for the Municipality of Gurabo to comply with requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality of Gurabo complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the fiscal year ended June 30, 2002.

Internal control over compliance

The management of the Municipality of Gurabo is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Municipality's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Municipality's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as finding 2002-8.

Hon. José A. Rivera Rodríguez
Mayor
Commonwealth of Puerto Rico
Municipality of Gurabo
Page 3

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider finding 2002-8 to be a material weakness.

Schedule of expenditures of federal awards

We have audited the general purpose financial statements of the Municipality of Gurabo as of and for the fiscal year ended June 30, 2002, and have issued our report thereon dated July 3, 2003. Our audit was performed for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the general purpose financial statements. Such information has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the general purpose financial statements taken as a whole.

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



Pannell Kerr Forster

License No. 22

Expires on December 1, 2004

July 3, 2003

SECTION 2 – FINANCIAL STATEMENT FINDINGS

Finding No. 2002-1

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Material Weakness Internal Control Structure Design
Questioned Cost:	None

Condition:

1. The general ledger fund and cash account balances as of June 30, 2002 as per OCAM System were misstated.
2. Cash at June 30, 2002 per general ledger control accounts were not in agreement with their corresponding bank reconciliations by \$3,559,317.

Criteria:

1. The Puerto Rico Municipal Law (Law 81) requires in its article number 8.010 that the Puerto Rico municipalities implement an accounting system that is in accordance with accounting principles generally accepted in the United States of America (GAAP). The law also requires that the accounting system to be implemented by the municipalities is the one developed and approved by the Office of the Commissioner of Municipal Affairs (OCAM by its abbreviation in the Spanish language).
2. The accounting principles contained in the Codification of Governmental Accounting and Financial Reporting Standards in section 1100 requires that a governmental accounting system must make it possible (1) to present fairly and with full disclosure the financial position and results of financial operations of the fund and account groups of the governmental unit in conformity with GAAP and (2) to determine and demonstrate compliance with finance-related legal and contractual provisions.

Cause: The cash reconciliation module of the OCAM System is not operational. Also, batches of accounting transactions were not posted in the general ledger causing that significant adjusting journal entries be proposed.

No adequate reconciliation procedures are being performed between amounts per bank reconciliations and general ledger cash accounts. In addition, no adequate communication channels exist between the Accounting, Remittances and Disbursement Areas.

Effect:

1. The Municipality is not in compliance with Article 8.010 of Law 81.
2. The Municipality has to prepare manual worksheets of analyses and reconciliations in order to maintain control over cash balances.
3. The OCAM accounting system is unable to produce reliable financial reports in benefit of management to monitor the Municipality's financial operations.
4. Significant adjustments were proposed in order to establish cash balances at June 30, 2002.

Recommendation: Since article 8.010 of Law 81 permits OCAM to approve the design and implementation of other accounting systems besides the one developed by them, we suggest the Municipality's management to request such authorization from OCAM. We also, suggest that the Municipality implements a financial accounting system that provides fiscal controls and accounting procedures that are:

1. In accordance with (GAAP) including:
 - a) Information pertaining to obligations, unobligated balances, assets, liabilities, expenditures, and income;
 - b) Effective internal controls to safeguard assets and assure their proper use;
 - c) A comparison of actual expenditures with budgeted amounts;
 - d) Source documentation to support accounting records; and
 - e) Proper charging of costs and cost allocation.
2. Sufficient to:
 - a) Permit the tracing of funds to a level of expenditures adequate to establish that funds have not been used in violation of the applicable restrictions on the use of such funds; and
 - b) Permit preparation of required reports, and eventually financial statements in accordance with
 - c)

We suggest that the Municipality's Finance Department performs monthly monitoring of the reconciliation process. Any difference between amounts per bank reconciliations and general ledger control accounts should be identified, investigated and adjusted in the general ledger on a timely basis. The performance of such procedures will aid in maintaining complete and accurate financial records and achieving more efficient procedures.

GASB Statement No. 34 (Basic Financial Statements and Management's Discussion and Analysis – for State and Local Government). The statement will have a significant effect on how the Municipality prepares its external financial statements for fiscal years beginning after June 15, 2003.

FINDING NO. 2002-1

Finding No. 2002-2

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Material Weakness Internal Control Structure Design
Questioned Cost:	None

Condition:

1. The accounting of special revenue and capital project funds are combined together in four (4) funds: 02 and 70 (special revenue funds) and 20 and 21 (capital project funds).
2. The Municipality does not account in the OCAM System the transactions related with the debt service fund.
3. The Municipality does not update in the OCAM System the trial balances of the General Fixed Asset and General Long-Term Debt account groups.
4. The Municipality did not record in the OCAM System the audit adjustments proposed for the Single Audit corresponding to fiscal year ended June 30, 2001.

Criteria: Puerto Rico municipalities should implement an accounting system that is in accordance with accounting principles generally accepted in the United States of America (GAAP). [Puerto Rico Municipality Law (Law 81) article number 8.010].

Specifically, Puerto Rico municipalities should record their financial transactions using fund accounting. [Puerto Rico Municipality Law (Law 81) article number 8.010(b)].

Generally accepted accounting principles applicable to governmental entities through its principles: NCGA Statement 1, NCGA Interpretation 5, GASB Statement 6, GASB Statement 9, GASB Statement 14, GASB Statement 25, GASB Statement 27 and GASB Statement 31, establish the statement of principles related to: (a) fund accounting systems, (b) types of funds, and (c) number of funds.

Cause: The personnel in charge of recording, processing the accounting transactions in the OCAM System did not monitor and provide for the initialization of such funds (self balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances) to permit that all individual special and capital projects activities to be recorded separately.

Effect: The Municipality has to maintain manual self balancing set of accounts for individual special and capital project activities included in the above mentioned funds in order to assure that the specific activities are carried and the objectives are attained in accordance with the special regulations, restrictions, or limitations for such transactions.

Recommendation: The Municipality must provide fiscal controls over accounting procedures that are in accordance with GAAP, including self-balancing set of accounts for all individual activities.

Governmental funds' long-term debts and liabilities are currently accounted for in the general long-term debt account group isolated from other government funds. GASB 34 will require the Municipality to record all debt and long-term liabilities within the related activity on the government-wide financial statements (e.g., governmental and business type activities). Additionally for government-wide financial statements, the new requirements will require the Municipality to record all liabilities at the time they are incurred (accrual basis of accounting) rather than when the transaction has an effect on current expendable resources (modified accrual basis of accounting). The Municipality's financial reporting system and related procedures may need to be modified to properly record debt and long-term liabilities in the appropriate activities and to convert from modified accrual basis of accounting to the accrual basis of accounting. Careful analysis of such matters should be performed in components of the denominated fund number 61 in the Municipality's general ledger (Bonds, Special Notes, Federal Notes, Accrued Compensated Absences and Accrued Legal Claims).

END FINDING NO. 2002-2

Finding No. 2002-3

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Material Weakness Internal Control Structure Design
Questioned Cost:	None

Condition: Interfund transactions were not balanced at June 30, 2002.

Criteria: Puerto Rico municipalities should implement an accounting system that is in accordance with generally accepted accounting principles. [Puerto Rico Municipality Law (Law 81) article number 8.010]

“.....because each fund is a fiscal and accounting entity, the amounts due to one fund from other funds, as well as the amounts owed to other funds, should be reflected in the fund accounts and in fund financial statements”. [GASB Cod. Sec. 1300.110]

Cause: Interfund transactions recorded incorrectly in the OCAM system.

Effect: The balances of interfund transactions were materially misstated at June 30, 2002.

Recommendation: We suggest that the Municipality's finance department performs monthly monitoring procedures over the status of the interfund transactions. A matrix listing the receivable funds on the left and the payable funds across the top can be useful for monitoring the status of the interfund transactions. An example of such a matrix is as follows:

INTERFUND TRANSACTION MATRIX

<u>Receivable Funds</u>	<u>Payable Funds</u>			<u>Enterprise</u>	<u>Total</u>
	<u>General</u>	<u>Special Revenue</u>	<u>Capital Projects</u>		
General Fund	XXX		5,000	5,000	10,000
Special Revenue	25,000	XXX	15,000		40,000
Capital Projects		10,000	XXX	10,000	20,000
Enterprise			5,000	XXX	5,000
Total	25,000	10,000	25,000	15,000	75,000

Funds reading across are due money from each of the Payable Funds listed at the top.

Funds reading down owe money to the Receivable Funds listed on the left.

At the end of the month, all interfund accounts should be verified against the matrix to determine whether they are still in agreement.

END FINDING NO. 2002-3

Finding 2002-4

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Material Weakness Internal Control Structure Design
Questioned Cost:	None

Condition: Federal grants and other non-general fund's non-exchange transactions were recorded as revenue when the resources were received instead of when the resources were available (susceptible to accrual) and measurable.

Criteria: Puerto Rico municipalities should implement an accounting system that is in accordance with GAAP. [Puerto Rico Municipality Law (Law 81) article number 8.010].

The GASB Statement No. 33 (Accounting for Certain Non-exchange Transactions) requires non-exchange transactions to be classified into one of the following 4 broad categories:

Derived tax revenues: result from the assessment imposed on exchange transactions (examples: sales taxes, personal and corporate taxes, motor fuel taxes and similar taxes on earnings or consumption).

Recognition:

- Assets: In the period when the underlying exchange has occurred or when the resources are received, whichever is first.
- Revenues: in the period when the underlying exchange has occurred. (Report advance receipts as deferred revenues). When modified accrual accounting is used, resources also should be available.

Imposed non-exchange revenues: Result from assessments by the governments or non-governmental entities (including individuals) that are not assessments on exchange transactions (examples: property taxes, most fines and forfeitures).

Recognition:

- Assets: period when an enforceable legal claim has arisen or when resources are received, whichever is first.
- Revenues: period when resources are required to be used or first period that use is permitted (for example, for property taxes, the period for which levied). When modified accrual accounting is used, resources also should be available.

Government mandated non-exchange transactions: Result when one level of government provides resources to a government at another level, requiring use of the resources for a specific purpose as established in enabling legislation (examples: federal government mandates on state and local governments).

Voluntary non-exchange transactions: Result from legislative or contractual agreements other than exchanges, entered into willingly by both parties.

Recognition:

- Assets and liabilities: period in when all eligibility requirements have been met or (for asset recognition) when the resources are received, whichever occurs first.

- Revenues and expenditures/expenses: Period when all eligibility requirements have been met (Report advance receipts or payments for use in the following period as deferred revenues or advances, respectively. However, when a provider precludes the sale, disbursement or consumption of resources for a specific number of years, until a specified event has occurred, or permanently [for example, permanent and term endowments], report revenues and expenses/expenditures when the resources are, respectively received or paid and report resulting net assets, equity, or fund balance as restricted). When modified accrual accounting is used for revenue recognition, resources also should be available.

Cause: The management of the Municipality has not devoted attention to the GASB Statement No. 33 through training programs.

Effect: The balance of deferred revenues, due from other governments, non-exchange revenues, and expenditures were significantly misstated in general ledger at June 30, 2002.

Recommendation: Management should analyze the contractual agreements formalized with external entities of non-general fund non-exchange items to ascertain the type of non-exchange transactions that apply in accordance with the provisions of GASB 33 (specially for government mandated and voluntary non-exchange transactions) before recording such financial transactions in the general ledger.

We suggest the implementation of formal training or continued professional education programs for the Finance Department personnel in governmental accounting and financial reporting topics.

END FINDING NO. 2002-4

Finding 2002-5

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Material Weakness Internal Control Structure Design
Questioned Cost:	None

Condition:

1. The Municipality does not record the expenditures of significant amounts of property and equipment purchased during the year 2001-2002 in all funds.
2. The Municipality does not record in the subsidiary of property, plant and equipment the expenditures related to the construction of capital assets in the general fixed assets account group as construction in progress, building, improvements and land acquisition when the expenditures are incurred.
3. The Municipality's management could not provide us with evidence that a physical inventory was performed.

Criteria: Puerto Rico municipalities should implement an accounting system that is in accordance with GAAP. [Puerto Rico Municipality Law (Law 81) article number 8.010].

The Revised Regulations of Basic Puerto Rico Municipalities Standards issued by OCAM, establishes in its Chapter VII (Custody, Control and Accounting of Municipality Property, section 22 (Annual Physical Inventory) that every municipality should maintain an adequate control of its property by the taking of periodic physical inventories (annually). As soon as the inventory listings are prepared the employee in charge of the municipal property should trace the listing totals against the accounting records. If differences exist between the listings and the accounting records a reconciliation and investigation must be performed.

Fixed assets other than those accounted for in the proprietary funds or trust funds are general fixed assets. General fixed assets are accounted for in the General Fixed Assets Account Group (GFAAG) rather than in the governmental funds. [NCGAS 1, p 38].

Cause: The Finance Department does not perform reconciliations between the total of capital outlay expenditures and the additions reported in the subsidiary of property, plant and equipment.

In addition, the employee in charge of the Municipal property does not perform periodic reconciliations of the property ledger (listing) with the General Fixed Asset Account Group control account as required by the municipal regulations issued by OCAM.

Effect:

1. The General Fixed Asset Account Group and total capital outlays were materially misstated at June 30, 2002.
2. The Municipality is not in compliance with the municipal regulations issued by OCAM.
3. The Property control procedures in place do not ensure adequate safeguards to prevent any loss, damage, or theft of the Municipality's property.
4. The financial statements of the Municipality as of June 30, 2002 were qualified because we were unable to apply the required auditing procedures over the general fixed assets.

Recommendation:

We suggest the implementation of a formal training program for the Finance Department's personnel in governmental accounting and financial reporting topics.

The Municipality should make the record keeping of the expenditures related to the construction of capital assets (buildings and improvements) in the general fixed assets account group as construction in progress when the expenditures are incurred.

On a monthly basis the construction in progress account in the general ledger should be reconciled against the construction subsidiary ledger maintained by the Department of Finance (after verifying its completeness, accuracy and reliability) and any differences investigated and/or adjusted as per the circumstances.

The Municipality needs to analyze periodically the details of all expenditure accounts terminated in codification 93.01 and 93.27 (Office equipment), 93.11 (Municipal vehicles), 99.99 (Payments of prior years' encumbrances) and 94.65 (Miscellaneous) for all funds in order to ascertain if expenditures of property units reconcile with the additions in the subsidiary of property, plant and equipment.

In addition, careful analysis should be performed in the following accounts related with acquisition of real property and construction of capital assets: 94.31 (Architectural and Engineering Fees), 94.32 (Construction costs), 94.33 (Relocation costs), Acquisition costs (94.34), 94.35 (Appraisal fees) and 94.41 (Inspection of buildings' constructions). Since we noted that significant costs, which are related with transactions that involve the acquisition, construction and development of capital assets as well as the attempts of the Municipality to begin investment processes to acquire real properties, are not capitalized and accounted for in the subsidiary of property, plant and equipment. The accounting of such capital asset transactions is necessary in order to maintain a comprehensive detail of property, plant and equipment.

GASB 34 will require the Municipality to account for all capital assets as part of the government's general and business type activities. This new requirement differs from current accounting standards that require the reporting of general government's capital assets into an account group in the combined balance sheet, i.e., General Capital Asset Account Group (GFAAG) currently does not mandate infrastructure assets or require the recording of depreciation expense. Capital assets include land, land improvements, easements, buildings, building improvements, vehicles, machinery, equipment, works of art and historical treasures, and all other tangible or intangible assets that are used in the Municipality's operations and that have initial useful lives extending beyond a single fiscal year. Examples of major infrastructure assets include roads, bridges, tunnels, drainage systems, water and sewer systems, lighting systems and other public works acquired since 1980.

Another capital asset that represents a challenge is the recognition of art collections and historical treasures. The Municipality has significant assets in this category and it will require special attention to the requirements of GASB 34 with regards to capitalization alternatives and depreciation.

Recording depreciation expense is also a new requirement. This requirement increases the importance of having a complete inventory listings of all capital assets. Without a complete record, the Municipality will not be able to record proper depreciation expense amounts, which in turn will result in improper fund and net asset balances. The Municipality does not maintain a comprehensive capital asset subsidiary. For financial reporting purposes, the Municipality must adopt and establish formal capitalization policies.

To comply with these new requirements, the Municipality will likely need to perform a complete inventory count of all capital assets, including infrastructure assets and works of art currently owned which have not previously been required to be recorded in the financial statements. Upon completion, the cost of these assets, adjusted for accumulated depreciation not previously recorded, will need to be determined and recorded in the accounting records. Depreciation expense must then be calculated and recorded along with the results of the inventory count. It is important that the Municipality maintains and updates capital asset subsidiaries on a timely basis in order to properly calculate and record capital assets and related depreciation.

END FINDING NO. 2002-5

Finding 2002-6

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Material Weakness Internal Control Structure Design
Questioned Cost:	None

Condition:

1. The total vouchers payable as of June 30, 2002 had misleading balances.
2. The detail of outstanding encumbrances for all funds was not reconciled with fund balance reserved for encumbrance control accounts.
3. The deferred volume of business tax revenue at June 30, 2002 was materially misstated by \$3,649,030.
4. The Municipality did not perform segregation between accounts payable and encumbrances.

Criteria: The Puerto Rico Municipality Law (Law 81) requires in its Article Number 8.010 that the municipalities' accounting systems provide fiscal controls and accounting procedures that are in accordance with GAAP, including effective internal controls to safeguard assets and assure their proper use.

Cause: The Municipality does not perform monthly reconciliations of the vouchers payable, deferred volume of business tax remittances and encumbrance's subsidiary ledgers for all funds with the vouchers' payable, deferred volume of business tax revenues and all-fund encumbrance control accounts, respectively. In the specific case of vouchers payable, the Municipality records the expenditures when the disbursement occurs rather than when the service is received (susceptible to accrual).

Effect: The Municipality's vouchers payable, deferred volume of business tax revenue and the encumbrance control accounts were misstated. Therefore, significant adjustments were required to establish the balance of said accounts at June 30, 2002.

Recommendation: The Municipality must perform monthly reconciliations of the vouchers payable, deferred volume of business tax revenue, and encumbrance subsidiary ledgers with their respective control accounts. Any difference between the subsidiary ledgers and the general ledger control accounts must be investigated and/or adjusted as required by the circumstances.

The Finance Department's personnel involved in the recording, processing and approval of transactions in the OCAM System must take in consideration that expenditures should be recognized in the period when the service was received (accrual basis of accounting), rather than when the disbursement is incurred (cash basis of accounting). At the same time the expenditure is properly recognized, a journal entry for reversing the associated encumbrance accounts should be made in the general ledger in order to make the required transition from the budgetary to the modified accrual basis of accounting.

Finally, the deferred volume of business tax revenue should be updated based on the remittances made during current year that are levied for the next fiscal year. This deferral should be reversed in the general ledger effective July 1 of the next accounting period.

END FINDING NO. 2002-6

Finding 2002-7

Program CFDA No. / Grant No.:	N/A
Type of Reportable Condition:	Internal Control Material Weakness Structure Design
Questioned Cost:	None

Condition: The following situations were observed regarding the human resource structure and functions in the Municipality:

1. The Finance Director does not have a password to access the OCAM Accounting System. Only one employee has unique access to the OCAM System, which is the same person that originates the general journal entries.
2. The Finance Department does not have an accounting supervisor. Therefore, there is no evidence that the general journal entries are reviewed and approved by a responsible official not involved with their origination.
3. Control and subsidiary accounts are not reconciled regularly and discrepancies are not reported to appropriate personnel.

Criteria:

The Puerto Rico Municipality Law (Law 81) requires in its article number 8.010 that the Puerto Rico municipalities' accounting systems (OCAM Systems) provide fiscal controls and accounting procedures that are in accordance with GAAP, including effective internal controls to safeguard assets and assure their proper use.

The Article 6.004 of the Law 81 establishes that the Internal Auditor, in addition to having a bachelor's degree in Business Administration with a Major in Accounting, should have at least 2 years of audit experience, preferable in the governmental area.

Article 6.005 of the Law 81 establishes that the Finance Director should supervise the tasks related with the preparation and completeness of financial reports.

Article 6.007 of the Law 81 establishes that the municipalities can establish systems and procedures to produce single reports in order to keep the Major aware about the economic situation and financial position of the municipality.

Cause:

1. Management has not demonstrated concern about and willingness to correct important weaknesses in the system of internal controls.
2. Absence of monitoring procedures regarding the reliability of the accounting data generated from the OCAM system.
3. Employees involved in the processing and recording of transactions in the OCAM system are not adequately trained to meet their assigned responsibilities.
4. Management has not established adequate and effective policies and procedures for the development, modification, and use of computer programs and data files.
5. Employees involved in the processing and recording of transactions in the OCAM system are not adequately supervised to ensure that they understand and perform in accordance with the GAAP.
6. Management is not aware of the existence of new accounting or reporting pronouncements and how they may affect the Municipality's financial reporting practices.
7. Management could not commit the appropriate human and financial resources to develop the necessary financial reporting information systems.
8. Internal control recommendations made by external auditors were not implemented.
9. Management has not examined the internal control system from time to time, nor evaluated its effectiveness.

Effect: Existence of material weaknesses in internal controls in terms of the recording, processing, supervision, authorization and monitoring of accounting data, which have a negative effect in the reliability of information produced by the OCAM system which is also relevant to the preparation of financial statements. As a result, the accounting system does not provide on a timely manner the necessary information for the preparation of financial statements and related disclosures in accordance with GAAP.

Recommendation: Management should design and be aware of training and continued professional education programs regarding internal control procedures over governmental audits and accounting, and over actual and new accounting procedures and technical releases that have a significant impact in the preparation of financial statements.

END FINDING NO. 2002-7

SECTION 3 – FEDERAL AWARDS FINDINGS

Finding 2002-8

Program CFDA No. / Grant No.:	14.871 Section 8 Rentals Programs for Low and Very Low Income Families 14.228 State Block Grant Program
Type of Reportable Condition:	Material Non-compliance – Equipment and real property management
Questioned Cost:	None

Condition:

1. During our review of the Municipality's property register in the OCAM System we noted that the Municipality does not segregate the list of properties purchased with Section 8 Rental Program and State Block Grant Program funds to determine the Municipality's compliance with each program's equipment and real property management.
2. The Municipality's management could not provide evidence that a physical inventory was performed.

Criteria: Compliance Supplement of Circular A-133, Part 3, section F (Equipment and Property Management) establishes that the local governments shall follow the A-102 Common Rule for equipment acquired with federal awards.

Circular A-102 (Common Rule), section .32 requires that property records must be maintained to include a description of property, serial number, or other identification number, the source of property, who holds the title, the acquisition date, cost of the property, percentage of federal participation in the cost of the property, percentage of federal participation in the cost of property and any ultimate disposition data including the date of disposal and sales price of the property.

Circular A-102, section .32(d)(2) establishes that a physical inventory of the property must be taken and the results reconciled with the property records at least once every two years.

Cause: The persons in charge of recording property in the accounting records do not identify the specific source of funds from which the acquisitions were made, nor perform a timely physical inventory. In addition the persons in charge of maintaining such registers do not understand the importance of such information.

Effect: The Municipality does not comply with the Equipment and Property Management criteria.

Recommendation: A physical inventory must be performed by the employees responsible of doing these tasks. Information obtained from the physical inventory should be compared with the subsidiary of property, plant and equipment and if differences result these should be documented, investigated and adjusted on a timely basis in order to have reliable records of property, plant and equipment.

Finally, specific instructions should be provided to personnel in charge of recording property acquisitions in order to identify the federal funds from which the equipment was acquired.

END FINDING NO. 2002-8

**REPORT ON THE STATUS OF UNCORRECTED
MATERIAL FINDINGS AND RECOMMENDATIONS
FROM PRIOR AUDITS THAT AFFECT THE FINANCIAL
STATEMENT AUDITS AS REQUIRED BY GOVERNMENT
AUDITING STANDARDS**

Finding 2001-1

Audit finding description:

1. *"The general ledger fund and cash account balances as of June 30, 2001 as per OCAM system were misstated."*
2. *"Cash at June 30, 2001 per general ledger control accounts were not in agreement with their corresponding bank reconciliations by \$9,006,233."*

Audit finding status:

Corrective action was not taken and same situation was mentioned in Audit Finding 2002-01.

Finding 2001-2

Audit finding description:

1. *"The accounting of special revenue and capital project funds are combined together in four (4) funds: 02 and 70 (special revenue funds) and 20 and 21 (capital project funds)."*
2. *"The Municipality does not account in the OCAM System the transactions related with the debt service fund."*
3. *"The Municipality does not update in the OCAM System the trial balances of the General Fixed Asset and General Long-Term Debt account groups."*

Audit finding status:

Corrective action was not taken and same situations were mentioned in Audit Finding 2002-02.

Finding 2001-3**Audit finding description:**

"Interfund transactions were not balanced at June 30, 2001."

Audit finding status:

Corrective action was not taken and same situation was mentioned in Audit Finding 2002-03.

Finding 2001-4**Audit finding description:**

"Federal grants and other non-general fund's non-exchange transactions were recorded as revenue when the resources were received instead of when the resources were available (susceptible to accrual) and measurable."

Audit finding status:

Corrective action was not taken and same situation was mentioned in Audit Finding 2002-04.

Finding 2001-5**Audit finding description:**

1. *"The Municipality does not record the expenditures of significant amounts of property and equipment purchased during the year 2000-2001 in all funds."*
2. *"The Municipality does not record in the subsidiary of property, plant and equipment the expenditures related to the construction of capital assets in the general fixed assets account group as construction in progress, building, improvements and land acquisition when the expenditures are incurred."*
3. *"At June 30, 2001 there was a difference of approximately \$6.6 million between the General Fixed Asset Account Group control account and the property subsidiary ledger."*
4. *"During our examination of the Municipality's property and equipment adjustments to eliminate property, plant and equipment from the subsidiary, the Municipality could not provide evidence of the disposal and retirement of \$2,491,814 of equipment and \$143,000 of land."*
5. *"The Municipality's management could not provide us with evidence that a physical inventory was performed."*

Audit finding status:

Corrective action was not taken and the same situations were mentioned in Audit Finding 2002-5.

Finding 2001-6**Audit finding description:**

1. *"The total vouchers' payable as of June 30, 2001 were materially misstated by \$1,811,085."*
2. *"The detail of outstanding encumbrances for all funds was not reconciled with fund balance reserved for encumbrance control accounts."*
3. *"The deferred volume of business tax revenue at June 30, 2001 was materially misstated by \$2,163,473."*
4. *"The Municipality did not perform segregation between accounts payable and encumbrances."*

Audit finding status:

Corrective action was not taken and the same situations were mentioned in Audit Finding 2002-6.

Finding 2001-7**Audit finding description:**

"The following situations were observed regarding the human resource structure and functions in the Municipality:

1. *"The Finance Director does not have password to access the OCAM Accounting System. Only one employee has unique access to the OCAM System, which is the same person that originates the general journal entries."*
2. *"The Finance Department does not have an accounting supervisor. Therefore, there is no evidence that the general journal entries are approved by a responsible official not involved with their origination."*
3. *"The Internal Auditor needs additional training and experience in governmental audit and accounting."*
4. *"Control and subsidiary accounts are not reconciled regularly and discrepancies are not reported to appropriate personnel."*
5. *"Management does not safeguard backup files of its financial data in a place outside the premises of the Municipality's central headquarters."*

Audit finding status:

Corrective action was taken for items No. 3 and 5 above.

Corrective action was not taken for items No. 1, 2 and 4 above.

Finding 2000-1**Audit finding description:**

"We noted that the Municipality of Gurabo is not keeping an accounting system as required by Generally Accepted Accounting Principles at present time. The general, capital project and special funds are kept on the cash basis of accounting. Also, the system used to record the purchase orders and contracts are not adequate; because does not provide for a segregation between the accounts payable and the encumbrances. In order to prepare the combined financial statements, we realized several adjusting entries to convert them to a modified accrual basis of accounting."

Audit finding status:

Corrective action was not taken and the same situation was mentioned though findings 2001-1 to 2001-7 and 2002-1 to 2002-7.

Finding 2000-2**Audit finding description:**

"During the audit we noted that:

- a. The additions to the property ledger had been recorded on the cash basis, instead on the accrual basis.*
- b. There is no supervision process established in order to verify if each department keeps adequate control of the property that is under its responsibility.*
- c. Expenditures for financing charges of issued long-term debts, and financing charges related to the property, plant and equipment had not been recorded in the property ledger.*
- d. There is no supervision process to verify if each department keeps adequate control of the inventory"*

Audit finding status:

Corrective action was not taken and the same situation was mentioned in Audit Finding 2002-5.

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS AS REQUIRED BY OMB CIRCULAR A-133

Finding 2001-8

Program:

Urban Development Action Grant.

Audit finding description:

1. *"During fiscal year ended June 30, 2001, the Municipality disbursed funds of the UDAG program to cover costs of professional services for the preparation of proposals to receive federal financial assistance from the Community Development Block Grant (CDBG) and Community Policing Services (COPS) Programs."*

<u>Contractor</u>	<u>Check Number</u>	<u>Program Funded</u>	<u>Cost</u>
Consulting Management Group	263	CDBG	\$ 13,150
Consulting Management Group	265	COPS	36,534
			<u>\$ 49,684</u>

2. *"During the fiscal year ended June 30, 2001, the Municipality disbursed \$53,024 of UDAG program funds, for which the corresponding payment vouchers and supporting documentation were not provided:"*

<u>Contractor</u>	<u>Check number</u>	<u>Cost</u>
Costanar General Contractors	21902	\$ 12,283
Alco Corporation	22499	3,441
Costanar General Contractors	21521	3,760
Costanar General Contractors	21951	14,620
Costanar General Contractors	21926	18,920
Total		<u>\$ 53,024</u>

Audit finding status:

Corrective action was not taken.

Finding 2001-9**Programs:**

Section 8 Rental Programs
State Block Grant Program
Urban Development Action Grant

Audit finding description:

1. *"During our review of the Municipality's property register we noted that the Municipality does not segregate the list of properties purchased with Section 8 Rental Program, State Block Grant Program and Urban Development Action Grant Program funds for us to determine the Municipality's compliance with each program's equipment and real property management."*
2. *"The Municipality's management could not provide evidence that a physical inventory was performed."*

Audit finding status:

Corrective action was not taken.

Finding 2001-10**Program:**

Urban Development Action Grant

Audit finding description:

1. *"During August 2000, the Municipality exempted to a contractor from the payment of accrued interest amounting to \$347,740 on a loan receivable that involved funds of the Urban Development Action Grant Program (UDAG) without notification of said transaction to the United States Housing and Urban Development Agency (HUD)."*
2. *"During September 2000, the Municipality disbursed \$58,470 (check no. 20712) of UDAG funds to Consulting & Management Group for the financial advisory services contracted in the evaluation of the transaction of the loan receivable mentioned above and which was the basis to authorize the transaction mentioned in the condition stated just above. This activity was not allowed under the provisions of Title I of the Housing Community Development Act of 1974."*

Audit finding status:

Corrective action was not taken.

Finding 2001-11**Program:**

Urban Development Action Grant

Audit finding description:

"During the year ended June 30, 2001, the Municipality disbursed monies for \$177,372 of the UDAG program for which no evidence was provided to us that the Municipality required the contractors the submission of the construction workers' payrolls as follows:"

<u>Contractor</u>	<u>Check number</u>	<u>Cost</u>
Quality Chemical	20979	\$ 30,382
Costanar General Contractor	21236	43,439
Costanar General Contractor	21902	3,860
Costanar General Contractor	21816	22,574
Constructora 2005	21321	47,977
Costanar General Contractor	21445	29,140
Total		<u>\$177,372</u>

Audit finding status:

Corrective action was not taken.

Finding 2002-2**Program:**

Section 8 Rental Programs for Low and Very Low Income Families.

Audit finding description:

"During our voucher test vouchers for \$107,183 were not available for examination."

Audit finding status:

Corrective action was not taken.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Fiscal Year Ended June 30, 2002

Federal Grantor	Program Title	Federal CFDA Number	Grant Number	Expenditures
US Department of Housing and Urban Development				
Pass-through the Office of the Commissioner of Municipal Affairs	State Block Grant Program	14.228	2001-000030	\$341,044
Direct programs	Housing Assistance Payment Programs for Low Income Families	14.871	RQ41V0	665,252
	Urban Development Action Grant	14.235	N/A	7,126
Department of Health and Human Services				
Pass-through Department of Family of Puerto Rico	Child Care and Development Block Grant (SENDEC)	N/A	123-2000-00612	183,615
	Housing Preservation Grant	N/A	6300506600043	7,930
Pass-through the Office for the Affairs of the Elderly	Office for the Affairs of the Elderly Program (OGAVE)	N/A	N/A	64,681
Pass-through the Office for the Affairs of the Youth	Office for the Affairs of the Youth Program (OAJ)- Prevention for Delinquency	16.592	2000-LB-VX-1085	39,009
US Department of Agriculture	Rural Economic and Community Development, Domestic Water System Loan and Grant	N/A	N/A	18,800

Pass-through Department of Education	Child and Adult Care Food Program	10.558	N/A	6,504
US Department of Justice Office (Office of Community Oriented Policing Services)				
Pass-through Commonwealth of Puerto Rico Office of the Governor of Puerto Rico	Community Oriented Policing Services	16.710	1999-SH-WX-0670	366,251
Total Expenditures				\$1,700,212

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Fiscal Year Ended June 30, 2002

NOTE 1 – RECONCILIATION OF FEDERAL AWARD EXPENDITURES

The Schedule of Federal Awards is a summary of the activity of the Municipality of Gurabo's federal award programs presented on the accrual basis of accounting as explained note 1 of the General Purpose Financial Statements. A reconciliation of amounts included in the Schedule of Expenditures of Federal Awards and the General Purpose Financial Statements (Special Revenue and Capital Project Funds) follows:

Total expenditures accounted in special revenue funds on general purpose financial statements	\$2,629,421
Total expenditures accounted in capital project funds on general purpose financial statements	511,469
Less: Total expenditures per schedule of expenditures of Federal Awards	<u>(1,700,212)</u>
Total non-federal expenditures accounted in the general purpose financial statements	<u>\$1,440,678</u>

CORRECTIVE ACTION PLAN

Contact Person:	Mr. Héctor E. Machín Nazario Internal Audit Director
Phone number:	(787) 737-8411
Fax:	(787) 737-5250

Finding 2002-8

Corrective Action Plan:

In the future we will segregate properties purchased with Section 8 Rental and State Block Grant Programs. Also we will perform an annual physical inventory of all Municipality's capital assets.

The results obtained from the inventory taken will be reconciled with the subsidiary of property and general ledger control account. Any difference noted will be investigated and corresponding adjustments will be made.

Persons Responsible:

- Mr. Quintilio Colón Díaz, Finance Director
- Mr. José R. González, Property Officer

Estimated Implementation Date:

Between July 2003 to June 2004.