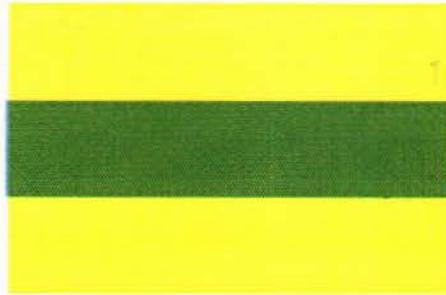


**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
ÁREA DE ASESORAMIENTO, REGLAMENTACIÓN E INTERVENCIÓN FISCAL
ÁREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE ISABELA
AUDITORÍA 2008-2009
30 DE JUNIO DE 2009**



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

***BASIC FINANCIAL STATEMENTS, REQUIRED
SUPPLEMENTARY INFORMATION
AND INDEPENDENT AUDITORS' REPORT
(WITH ADDITIONAL REPORTS REQUIRED UNDER
THE OMB CIRCULAR A-133)***

***AS OF AND FOR THE FISCAL YEAR ENDED
JUNE 30, 2009***



***Hon. Carlos Delgado-Altieri
Mayor***

***Mrs. Rosario M. Villanueva-Bravo
Finance and Budget Director***

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

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FINANCIAL SECTION

VALDES, GARCIA, MARIN & MARTINEZ, LLP

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS
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INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Isabela (the Municipality) as of and for the year ended June 30, 2009, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control over financing reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Isabela as of June 30, 2009 and for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated December 23, 2009, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

The Management Discussion and Analysis on pages 3 through 15 and Budgetary Comparison Schedule - General Fund on page 53 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements. The combining financial statements of the general fund are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, "Audits of States, Local Governments and Non-Profit Organizations", and is not a required part of the basic financial statements of the Municipality. The combining financial statements of the general fund and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The Financial Data Schedule supplementary information required by the Uniform Financial Reporting Standards of the Department of Housing and Urban Development on pages 56 through 58 has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Valdez, Garcia, Marin & Martinez LLP

San Juan, Puerto Rico
December 23, 2009

Stamp 2474904 was affixed
to the original.

MANAGEMENT'S DISCUSSION AND ANALYSIS

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

The following discussion will provide an overview of the Municipality's financial activities for the fiscal year ended June 30, 2009 through an analysis of the financial performance of the Municipality of Isabela. Please read it in conjunction with the financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

Highlights for Government-wide Financial Statements

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

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2009 by \$58,162,963 (net assets).
- Unrestricted net assets amount to \$4,881,866 in comparison to \$1,820,749 on year 2008.
- Revenues decreased by 0.15% and expenses decreased 7% in comparison with year 2008.
- Net change in net assets amounted to \$6,633,421, an increase of 30% with respect to prior year's net change.

Highlights for Fund Financial Statements

Detailed information about the Municipality's most significant funds is presented in the funds financial statements, which use the current financial resources measurement focus and modified accrual basis of accounting:

- At June 30, 2009, a net change of \$4,162,684 in the fund balances of the Municipality's governmental funds resulted in combined ending fund balances of \$31,887,271. Approximately 48% of the total combined fund balances is unreserved.
- The General Fund reported an excess of revenues and other financing sources over expenditures and other financing uses of \$2,225,098 and an unreserved fund balance of \$15,651,570. Unreserved fund balance increased 19% from prior year.

General Financial Highlights

- The investment in capital assets as of June 30, 2009 was \$42,217,913 (net of depreciation).
- Long-term debt increased to \$18,417,344.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$1,727,959.

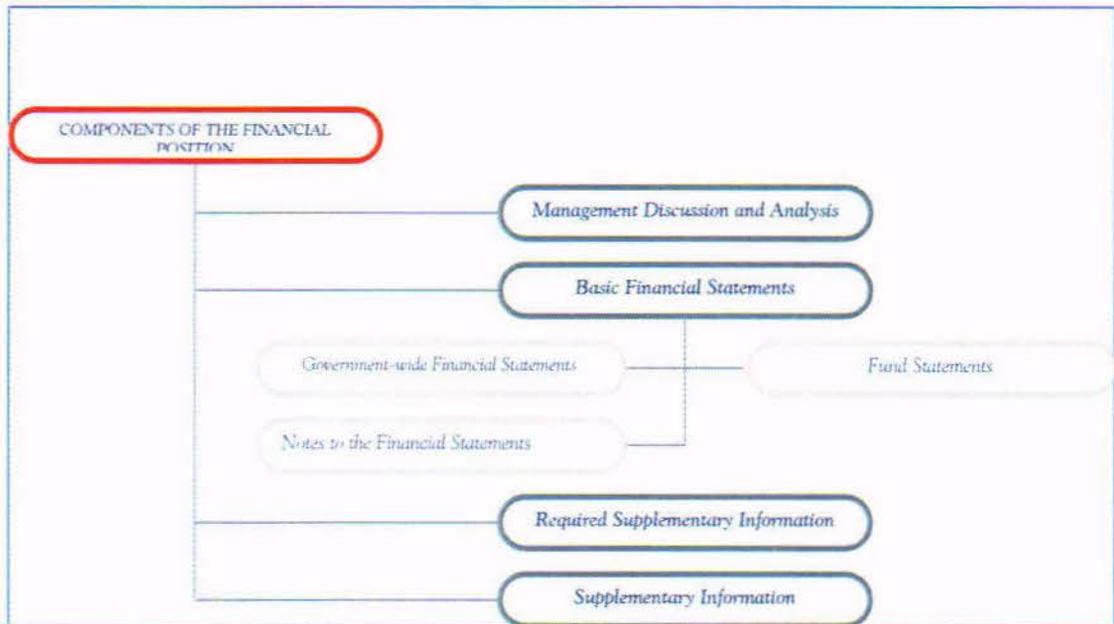
COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

OVERVIEW OF THE FINANCIAL STATEMENTS

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



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

Basic Financial Statements

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

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

- ***Fund Financial Statements***

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

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

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

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

The basic financial statements also include notes to explain information in the financial statements and provide more detailed data.

Required supplementary information

The statements and notes are followed by the required supplementary information that contains the budgetary comparison schedule for the General Fund.

Supplementary information

The supplementary information includes a financial data schedule containing financial information of the Section 8 Housing Choice Voucher Program administered by the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

The following table presents a summary of the Statements of Net Assets as of June 30, 2009 and 2008:

TABLE 1

<i>Summary Statement of Net Assets As of June 30,</i>		
	Governmental Activities	
	2009	2008 (as restated)
Assets		
Current and other assets	\$ 39,133,825	\$ 35,332,027
Capital assets	42,217,913	39,771,272
Total assets	\$ 81,351,738	\$ 75,103,299
Liabilities		
Current and other liabilities	\$ 4,771,431	\$ 5,671,167
Long-term liabilities	18,417,344	17,902,590
Total liabilities	23,188,775	23,573,757
Net assets		
Invested in capital assets, net of related debt	37,976,666	36,619,599
Restricted	15,304,431	13,089,194
Unrestricted	4,881,866	1,820,749
Total net assets	\$ 58,162,963	\$ 51,529,542

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. Net assets for the year increased 13% with respect to prior year.

The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure); less accumulated depreciation and less any related outstanding debt used to acquire those assets. The Municipality uses these assets to provide services to its citizens and consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other sources, because capital assets are not generally liquidated for the purpose of retiring debt.

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

Unrestricted net assets are the part of the net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements. As of June 30, 2009 the Municipality presented a \$4,881,866 surplus due to positive net change in net assets results for the year then ended.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

Changes in net assets

The following table summarizes the changes in net assets for the years ended June 30, 2009 and 2008:

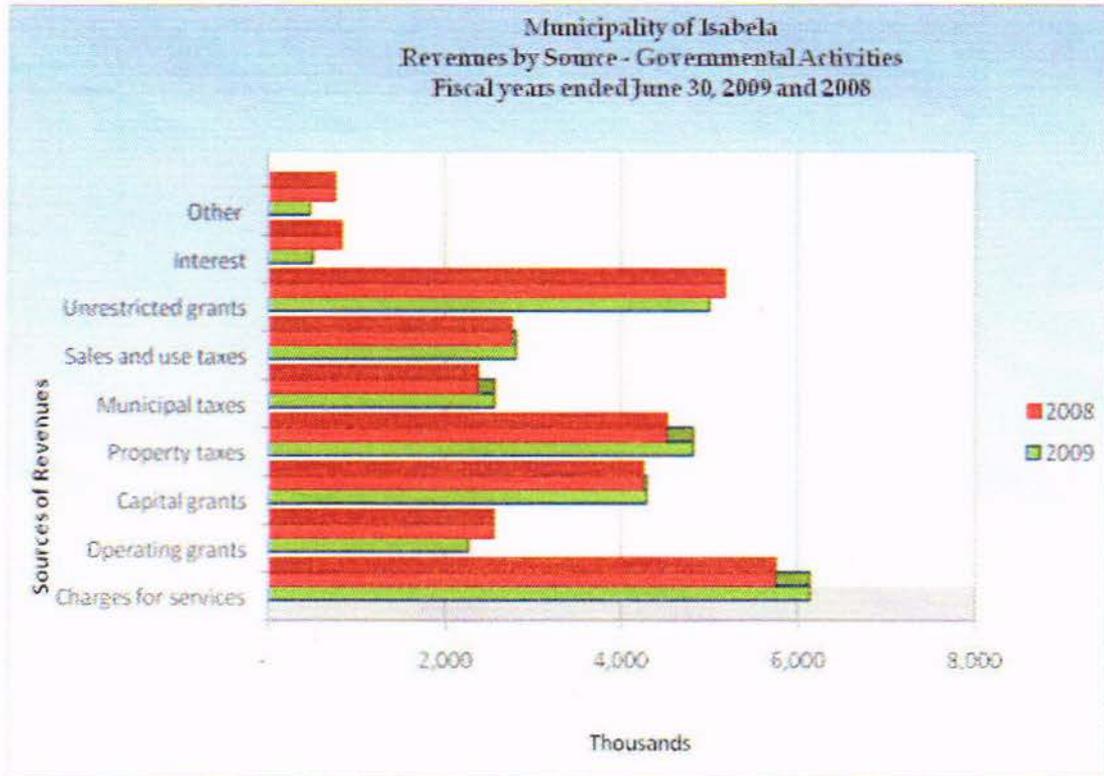
TABLE 2

<i>Summary of Change in Net Assets As of June 30,</i>		
	Governmental Activities	
	2009	2008 (as restated)
Program revenues:		
Fees, fines and charges for services	\$ 6,142,349	\$ 5,750,742
Operating grants and contributions	2,274,805	2,556,358
Capital grants and contributions	4,298,499	4,251,052
General revenues:		
Property taxes	4,823,579	4,517,124
Municipal license taxes	2,572,534	2,374,984
Sales and use taxes	2,814,933	2,759,156
Grants and contributions not restricted to specific programs	5,005,790	5,169,102
Interest	508,637	828,434
Other	478,440	529,470
Gain on disposition of capital assets	-	226,487
Total revenues	28,919,566	28,962,909
Expenses:		
General government	9,316,528	10,105,115
Public works and sanitation	3,598,173	4,736,968
Public safety	1,124,283	1,077,097
Culture and recreation	1,215,912	1,140,508
Health	2,803,578	3,074,707
Housing, welfare and community development	2,715,396	2,149,553
Education	1,184,836	1,107,586
Interest on long term debt	327,439	455,000
Total expenses	22,286,145	23,846,534
Change in net assets	6,633,421	5,116,375
Net assets-beginning of year	51,529,542	46,413,167
Net assets-end of year	\$ 58,162,963	\$ 51,529,542

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA
MANAGEMENT DISCUSSION AND ANALYSIS**

Fiscal year ended June 30, 2009

FIGURE 1



Approximately 21% of the Municipality's revenues came from fees and charges for services, 15% from capital grants, 17% from property taxes and 17% from unrestricted grants. The Municipality's expenses cover a range of services. The largest expenses are general government representing approximately 42%, public works and sanitation with 16%, health with 13% and housing, welfare and community development with 12%. Program revenues of the Municipality covered 57% of total expenses.

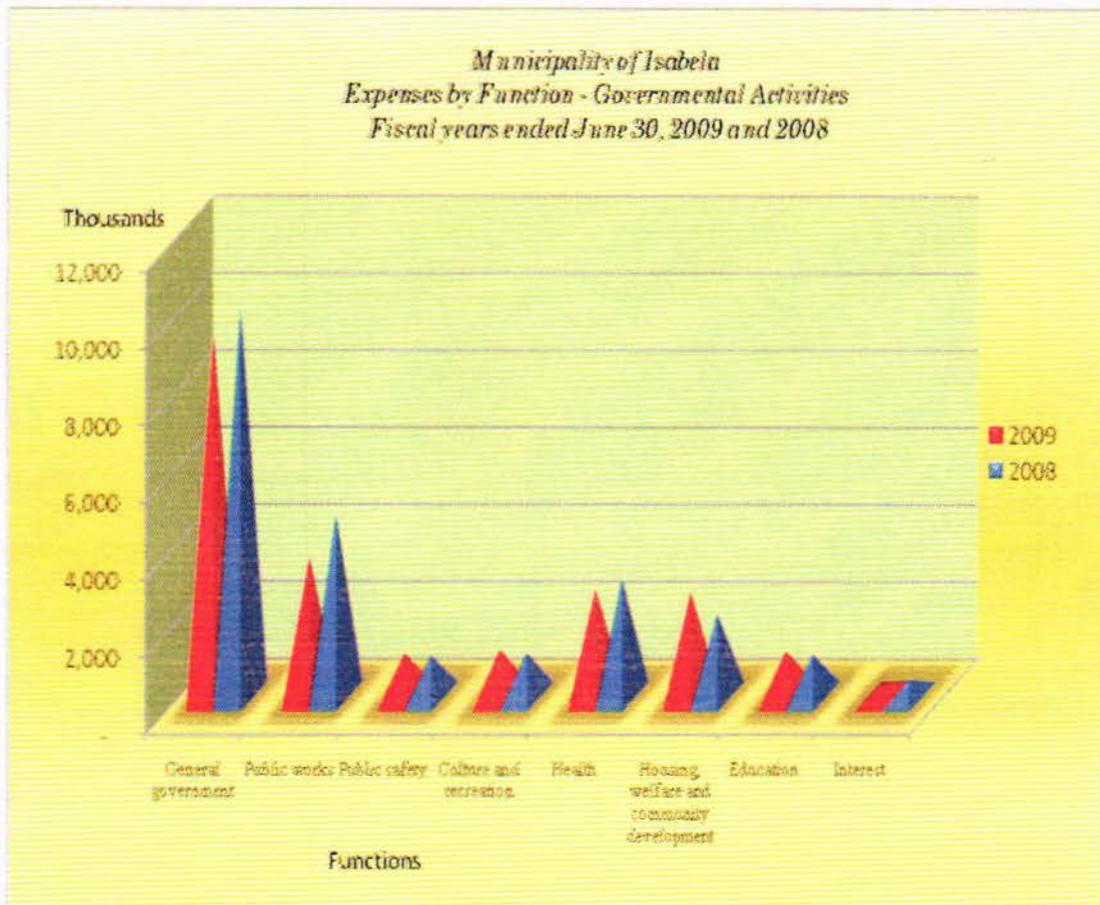
With respect to prior year, revenues reported a net decrease of approximately 0.15%. This net decrease is primarily the result of: (1) a 7% increase in fees, fines and charges for services due to an increase of 30% in construction permits; (2) a 7% increase in property taxes due to a positive CRIM FY 07-08 final liquidation; (3) an 8% increase in municipal license tax; (4) an 11% decrease in operating grants due to a 48% and 97% decrease in grants from the P.R. Department of Labor (Law 52 & Law 82) and the P.R. Department of Transportation, respectively, which were offset by a 53% increase in federal grants received from Homeland Security and a 29% increase in grants received from the P.R. Department of Family and the P.R. Office of the Elderly; (5) 39% decrease in interest revenue due to a significant decline in the interest rates earned on the certificates of deposit; and (6) finally, a 37% decrease in other revenue due to the inclusion in last year's government-wide financial statements of a gain on the disposition of capital assets in the amount of \$226,487.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

FIGURE 2



Expenses decreased 7% in comparison with 2008 year. Significant decreases were registered on interest on long-term debt with 26%, public works with 24%, health with 9% and general government with 8%, which were partially offset by a 26% increase in housing, welfare and community development. The decreases in those functions were caused mainly by a 28% decrease in the interest paid on the general obligation debt; an 11% decrease in the expenses incurred by the CIMA hospital; a significant decrease in the costs incurred for road maintenance; and to a positive adjustment in the municipal landfill obligation estimate. The 26% increase in housing, welfare and community development is the result of a significant increase in the expenses incurred in the home rehabilitation program funded by the CDBG Entitlement federal grant.

As noted previously the minimal decrease in revenues and the significant decrease in expenses caused an increase of 30% in the net change in net assets with respect to prior year net change.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

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

TABLE 3

<i>Net Cost of Municipality's Governmental Activities Fiscal years ended June 30,</i>				
Functions/Programs	Total Cost of Services		Net Cost of Services	
	2009	2008 (as restated)	2009	2008 (as restated)
General government	\$ 9,316,528	\$ 10,105,115	\$ 4,786,513	\$ 5,571,612
Public works and sanitation	3,598,173	4,736,968	663,867	1,024,711
Public safety	1,124,283	1,077,097	918,456	942,187
Culture and recreation	1,215,912	1,140,508	738,004	1,129,358
Health	2,803,578	3,074,707	695,848	1,107,697
Housing, welfare and community development	2,715,396	2,149,553	1,003,131	709,011
Education	1,184,836	1,107,586	437,234	348,806
Other	327,439	455,000	327,439	455,000
	<u>\$ 22,286,145</u>	<u>\$ 23,846,534</u>	<u>\$ 9,570,492</u>	<u>\$ 11,288,382</u>

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

Some of the cost of governmental activities was paid by those who directly benefited from the programs (\$6,142,349) and other governments and organizations that subsidized certain programs with grants and contributions (\$6,573,304). The \$9,570,492 net cost of services was fully covered by other general revenues including taxes and other grants and contributions not restricted to specific programs.

Governmental funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year. For the fiscal year ended June 30, 2009, the governmental funds reported combined ending fund balances of \$31,887,271, a net increase of \$4,162,684 in comparison with the prior year. This increase was caused primarily by a net change in the general fund of \$2,225,098, \$965,794 in the debt service fund and \$1,200,607 in other governmental funds. Of total combined fund balances, \$15,434,899 (48%) constitutes unreserved fund balance. The remainder of fund balance is reserved to indicate that is not available for new spending.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

The general fund is the operating fund of the Municipality. For the year ended June 30, 2009, the fund balance of the general fund increased by \$2,225,098 when compared with the prior year. Of this net change, \$151,280 pertains to special funds included as part of the general fund. The principal components of the net increase of \$583,605 in revenues are an increase of \$539,582 in property taxes; an increase of \$192,776 in municipal license tax; an increase of \$446,115 in fees, fines and charges for services; a decrease of \$416,599 in intergovernmental revenue; and a \$176,616 decrease in interest. The significant increase in property taxes is mainly the result of the inclusion in the 2008-2009 financial statements of \$283,990 in property tax revenue from prior years and to an 11% increase in the property tax collected during the fiscal year. The increase in fees, fines and charges for services is the result of a \$283,894 increase in construction permits and a \$147,021 increase in the revenues generated by the CIMA hospital. The \$416,599 decrease in intergovernmental revenues is the result of a \$260,563 decrease in the municipal subsidies and equalization fund sent by CRIM and a \$243,677 decrease in the grants received from the PR Department of Labor under the Law 52 and Law 82 payroll reimbursement programs. The net increase in expenditures of \$404,255 is due to an increase of \$478,836 in general government; an increase of \$233,846 in public works; and a decrease of \$317,876 in capital outlays. The significant increase in general government is the result of the expenditure of several designated funds created for various miscellaneous projects and for the payment to the U.S. Department of Housing and Urban Development of \$119,160 in disallowed costs incurred under the CDBG Entitlement grant program.

GENERAL FUND BUDGETARY HIGHLIGHTS

The general fund original budget for the fiscal period 2008-2009 presented an increase of 4% with respect to prior year budget. Amendments to the original budget are approved by the Municipal Legislature. During the fiscal year budget revenues were increased by \$1,990,625 due to additional collections of property tax, sales and use taxes, charges for services (mainly construction permits), and municipal license tax. However, budget transfers-out were increased by the same amount. Actual revenues exceeded the revised budgeted revenues by \$965,230 (net). The most significant variances were in sales and use taxes, \$287,401; intergovernmental revenue, \$285,544; interest, \$251,536 and other, \$145,418.

A positive variance of \$762,729 between revised budget and actual expenditures was due mainly to net decreases in the following functions: \$469,557 in general government, \$85,575 in public works and sanitation, and \$121,382 in housing, welfare and community development expenditures. The Municipality reported less expenditure (net) than appropriations in those functions on payments for salaries and fringe benefits. Actual revenues exceeded actual expenditures by \$1,727,959.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets

At the end of the fiscal year, the Municipality has invested \$42,217,913 (net of accumulated depreciation) in a broad range of capital assets, including buildings, parks, roads, bridges, land and equipment. This amount represents a net increase of approximately 6% over the prior year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

TABLE 4

<i>Capital Assets, net As of June 30,</i>			
	Governmental Activities		
	2009		2008 (as restated)
Non-depreciable assets:			
Land	\$	4,127,389	\$ 4,055,589
Construction in progress		5,589,828	5,823,626
Depreciable assets:			
Land improvements		14,186	14,479
Leasehold improvements		345,627	383,519
Buildings and buildings improvements		16,125,108	13,841,788
Infrastructure		11,652,343	10,856,436
Vehicles, machinery and equipment		4,363,432	4,795,835
Total	\$	42,217,913	\$ 39,771,272

The Municipality's major capital projects that were still in construction as of June 30, 2009 are as follows:

- Renovation of City Hall - \$2,706,106
- Improvements to the downtown electrical infrastructure - \$1,429,746
- Construction of Youth Sport and Educational Center - \$555,416
- Construction of "Parque Lineal Zona Costera" - \$704,481

Construction in progress decreased due to the completion of the construction projects "Parque Urbano Pablo Pérez" First Phase, road improvements Florida Community, and improvements to the Tocones' community center and basketball court for a total amount of \$3,001,196. However, these retirements were offset by the significant costs incurred in the renovation of City Hall, "Parque Urbano," "Paseo Lineal" and Youth Center projects, which total additions for 2008-2009 amounted to \$2,753,893.

The Municipality reported approximately \$1,068,120 in infrastructure additions during the year, which are composed mainly of capital improvements.

The Municipality acquired a total of \$315,041 of equipment during the fiscal year 2008-2009, including vehicles and several communications, surveillance and security equipment purchased with Homeland Security grant funds for the use of the municipal emergency management department for a total amount of \$239,156.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

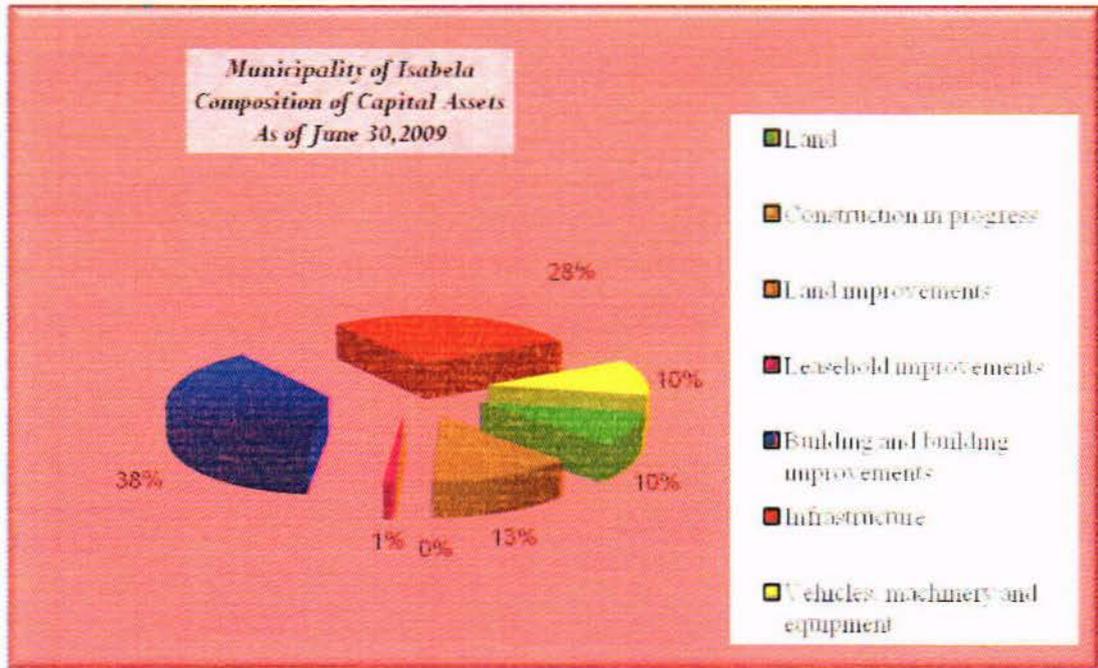
MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

The Municipality's fiscal year 2009-2010 consolidated capital budget calls for a significant amount of new and continuous projects including the completion of the renovation of the City Hall, construction of "Parque Lineal Zona Costera," construction of a new Youth Sport and Educational Center, improvements to the downtown electrical infrastructure, commencement of the second phase of the "Parque Urbano Pablo Pérez" project, purchase of land in the Jobos beach for its development into a recreational area; and the creation of a "poblado" in the Planas Community. These projects will be financed through Federal and Commonwealth grants, funds from the Commonwealth Legislature, general obligation bonds and Municipal funds.

Capital assets composition as of June 30, 2009 follows:

FIGURE 3



More detailed information about the Municipality's capital assets is presented in Note G to the financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

Long-term debt

At year-end, the Municipality had \$8,779,024 in general and special bonds and notes, an increase of 14% with respect to prior year. The following is a summary of the Municipality's outstanding debt as of June 30, 2009 and 2008:

TABLE 5

<i>Outstanding Long-term Debt</i>			
<i>As of June 30,</i>			
	Governmental Activities		
	2009	2008	
General and special obligation bonds and notes	\$ 8,779,024	\$ 7,680,024	
Note payable to CRIM – LIMS	159,564	217,123	
Note Payable to CRIM – prior years delinquent accounts	66,248	69,128	
Note payable to Puerto Rico Department of Labor	-	59,619	
Note payable to Puerto Rico Solid Waste Authority	98,545	134,905	
Note payable to Puerto Rico Treasury Department	313,416	458,778	
Note payable to PR Employee Retirement System Administration	59,110	114,554	
Note payable-Section 108 Loan Guarantee	1,200,000	1,200,000	
Landfill obligation	4,319,525	4,649,489	
Compensated absences	2,692,772	2,545,681	
Christmas Bonus	401,898	361,016	
Claims and judgments	3,000	150,000	
Payable to CRIM – property tax advances	49,056	50,514	
Payable to PREPA	275,186	211,759	
Total	\$ 18,417,344	\$ 17,902,590	

The increase in the general and special obligation bonds and notes is due to the issuance of a \$1,325,000 bond for the purchase of heavy equipment and municipal vehicles. In addition, the increase in the notes payable with Puerto Rico Electric Power Authority (PREPA) is the result of an excess of the annual energy charges incurred by the Municipality over the contribution in lieu of taxes ("CELI") for the fiscal year 2007-2008, which was recorded both a long-term debt and an account receivable from the agency. More detailed information about the Municipality's long-term liabilities is presented in Note I to the financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2009

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2009-2010 budget. One of these factors is the economy. Among economic areas considered are the population growth estimates, personal income, housing statistics and unemployment rates. The Municipality's unemployment rate now stands at 16.5%, which compares reasonably with the Commonwealth rate of 15.2%.

The Municipality applied a conservative approach in the development of budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2009-2010 are \$14,858,154, a decrease of approximately 2% with respect to prior year estimates. Budgeted expenditures are expected to be reduced accordingly to the decrease of budgeted revenues. In addition to the estimated budget for the general fund, the Municipality has submitted Federal and Commonwealth funds proposals for welfare and community development as well as for capital improvements and public works funds.

CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and creditors with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability for the money it receives. If you have questions about this report or need additional information, contact the Municipality's Director of Finance at PO Box 507, Isabela, Puerto Rico 00602.

BASIC FINANCIAL STATEMENTS

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

**STATEMENT OF NET ASSETS
JUNE 30, 2009**

ASSETS	<u>Governmental Activities</u>
Cash and investments	\$ 17,844,416
Receivables, net:	
Municipal License Taxes	4,774
Sales and use taxes (note M)	296,713
Other (note D)	286,921
Due from:	
Commonwealth Government (note E)	1,948,747
Federal Government (note E)	1,190,678
Restricted assets:	
Cash and investments	9,554,785
Cash with fiscal agent	6,879,417
Investment held with fiscal agent (note C)	756,822
Deferred charges	46,131
Inventories and Supplies	203,557
Other assets	120,864
Capital Assets (note G):	
Land and construction in progress	9,717,217
Other capital assets, net	32,500,696
	<u>42,217,913</u>
Total assets	<u><u>\$ 81,351,738</u></u>
LIABILITIES	
Accounts payable and accrued liabilities	\$ 2,311,361
Interest payable	104,977
Due to:	
Commonwealth Government (note E)	127,039
Federal Government	119,160
Deferred revenues:	
Municipal license taxes	2,005,528
Federal grants	1,495
Other	101,871
Long-term liabilities (note I):	
Due within one year	1,676,287
Due in more than one year	16,741,057
Total liabilities	<u>23,188,775</u>
NET ASSETS	
Invested in capital assets, net of related debt	37,976,666
Restricted for:	
Capital projects	7,952,447
Debt service	3,879,601
Other specified purposes	3,472,383
Unrestricted	4,881,866
Total net assets	<u><u>\$ 58,162,963</u></u>

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

STATEMENT OF ACTIVITIES
FISCAL YEAR ENDED JUNE 30, 2009

Functions	Expenses	Program Revenues			Net (Expenses) Revenues and Change in Net Assets
		Fees, Fines and Charges for services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
General government	\$ 9,316,528	\$ 4,000,363	\$ 260,751	\$ 268,901	\$ (4,786,513)
Public works and sanitation	3,598,173	31,456	34,078	2,868,772	(663,867)
Public safety	1,124,283	-	205,827	-	(918,456)
Culture and recreation	1,215,912	2,800	25,108	450,000	(738,004)
Health	2,803,578	2,107,730	-	-	(695,848)
Housing, welfare and community development	2,715,396	-	1,001,439	710,826	(1,003,131)
Education	1,184,836	-	747,602	-	(437,234)
Interest on long-term debt	327,439	-	-	-	(327,439)
Total	\$ 22,286,145	\$ 6,142,349	\$ 2,274,805	\$ 4,298,499	(9,570,492)
General revenues:					
Taxes:					
					4,823,579
					2,572,534
					2,814,933
					5,005,790
					508,637
					478,440
					<u>16,203,913</u>
					6,633,421
					<u>51,529,542</u>
					<u>\$ 58,162,963</u>

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2009

Assets	Major Funds						Total Governmental Funds
	General	Community Development Block Grant	Head Start	Debt Service	Commonwealth Legislature Resolutions	Other Governmental Funds	
Cash and investments	\$ 17,844,416	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 17,844,416
Receivables, net:							
Municipal License Taxes	4,774	-	-	-	-	-	4,774
Sales and use taxes	227,472	-	-	69,241	-	-	296,713
Other	255,214	-	-	-	6,799	24,910	286,923
Due from:							
Commonwealth Government	941,757	-	-	228,763	291,332	486,895	1,948,747
Federal Government	-	526,216	149,070	-	-	515,392	1,190,678
Other funds (note F)	1,893,821	-	-	-	33,545	9,068	1,936,434
Advances to other funds (note F)	-	-	-	-	1,307,497	-	1,307,497
Inventories and Supplies	203,557	-	-	-	-	-	203,557
Restricted assets:							
Cash and investments	157,106	1,495	1,626	-	2,829,469	6,565,089	9,554,785
Cash with fiscal agent	-	-	-	5,005,271	-	1,874,146	6,879,417
Investment held with fiscal agent	-	-	-	-	-	756,822	756,822
Total assets	\$ 21,528,117	\$ 527,711	\$ 150,696	\$ 5,303,275	\$ 4,468,642	\$ 10,232,322	\$ 42,210,763
Liabilities and Fund Balances							
Liabilities:							
Accounts payable and accrued liabilities	\$ 784,021	\$ 468,383	\$ 21,184	\$ -	\$ 325,748	\$ 712,027	\$ 2,311,363
Matured bonds and interest payable	-	-	-	444,358	-	-	444,358
Due to:							
Commonwealth Government	127,039	-	-	-	-	-	127,039
Federal Government	119,160	-	-	-	-	-	119,160
Other funds	9,068	57,833	129,512	-	-	1,740,021	1,936,434
Advances from other funds	1,307,497	-	-	-	-	-	1,307,497
Deferred revenues (notes H, I, and M):							
Municipal license taxes	2,010,302	-	-	-	-	-	2,010,302
Sales and use tax	24,374	-	-	16,408	-	-	40,782
Commonwealth Government	800,742	-	-	-	142,264	410,827	1,353,833
Federal grants	-	218,166	-	-	-	279,028	497,194
Other	173,280	-	-	-	1,347	903	175,530
Total liabilities	5,355,483	744,382	150,696	460,766	469,359	3,142,806	10,323,492
Fund balances (deficit):							
Reserved for:							
Inventories	203,557	-	-	-	-	-	203,557
Encumbrances	182,444	-	-	-	-	-	182,444
Debt service	-	-	-	4,842,509	-	-	4,842,509
Capital projects	-	-	-	-	2,567,760	5,666,744	8,234,504
Other specific purposes	135,063	-	-	-	124,026	1,422,772	1,681,861
Advances	-	-	-	-	1,307,497	-	1,307,497
Unreserved:							
Designated for future years expenditures	3,688,991	-	-	-	-	-	3,688,991
Undesignated	11,962,579	(216,671)	-	-	-	-	11,745,908
Total fund balances (deficit)	16,172,634	(216,671)	-	4,842,509	3,999,283	7,089,516	31,887,271
Total liabilities and fund balances	\$ 21,528,117	\$ 527,711	\$ 150,696	\$ 5,303,275	\$ 4,468,642	\$ 10,232,322	\$ 42,210,763

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

RECONCILIATION OF TOTAL GOVERNMENTAL FUND BALANCES
TO NET ASSETS OF GOVERNMENTAL ACTIVITIES
JUNE 30, 2009

Total governmental fund balances:	\$	31,887,271
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds:		42,217,913
Other assets used in governmental activities are not financial resources and therefore are not reported in the funds:		
Deferred charges:	\$ 46,131	
Other assets	120,864	166,995
Other assets are not available to pay for current-period expenditures and therefore are deferred in the funds:		
Receivables:		
Intergovernmental subsidy prior years - General Fund	73,219	
Municipal license tax	4,774	
Construction permits	38,194	
Charges for services	47,535	
Interest	2,250	
Sales and use tax - Municipal Development Fund	24,374	
Sales and use tax - Debt Service Fund Fund	16,408	
Due from Commonwealth Government:		
P.R. Department of Labor (Law No. 52 and 82)	21,752	
P.R. Department of Education	175,000	
P.R. Electric Power Authority (PREPA)	275,186	
P.R. Infrastructure Financing Authority	142,264	
P.R. Department of Correction and Rehabilitation	27,760	
Christmas Bonus Reimbursement	186,669	
Grant from P.R. Solid Waste Authority	6,005	
Grant from P.R. Department of Transportation	224,778	
Grant from Rural Development Corporation	123,747	
Grant from P.R. Department of Family - Pres	83,133	
Due from Federal Government:		
Federal Grant- Homeland Security	32,210	
Federal Grant-State and Community Highway Safety	20,540	
Federal Grant-Child Care	226,278	
Federal Grant-CDBG	216,671	1,968,747
Interest liabilities are not due and payable in the current period and therefore, are not reported in the funds:		(15,619)
Long term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds:		
General obligation bonds and notes	8,424,024	
Note payable to CRIM-LIMS	159,564	
Note payable to CRIM-financing of delinquent accounts	66,248	
Note payable to P.R. Solid Waste Authority	98,545	
Note payable to P.R. Treasury Department	313,416	
Note payable to Employees Retirement System	59,110	
Note payable to HUD-Section 108 Loan Guarantee	1,200,000	
Payable to PREPA	275,186	
Compensated absences	2,692,772	
Judgments and legal claims	3,000	
Christmas Bonus	401,898	
Estimated solid waste landfill closure and post-closure costs	4,319,525	
Payable to CRIM-excess of property tax advances	49,056	(18,062,344)
Net assets of governmental activities:	\$	<u>58,162,963</u>

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES-
GOVERNMENTAL FUNDS
FISCAL YEAR ENDED JUNE 30, 2009

	Major Funds						Total Governmental Funds
	General	Community Development Block Grant	Head Start	Debt Service	Commonwealth Legislature Resolutions	Other Governmental Funds	
Revenues:							
Taxes:							
Property taxes (note K)	\$ 3,577,940	\$ -	\$ -	\$ 1,308,047	\$ -	\$ -	\$ 4,885,987
Municipal license taxes (note L)	2,567,760	-	-	-	-	-	2,567,760
Sales and use taxes (note M)	2,479,233	-	-	331,098	-	-	2,810,331
Intergovernmental:							
Commonwealth government (note N)	7,212,488	-	-	-	733,681	1,496,102	9,442,271
Federal government	-	1,993,532	747,602	-	-	1,151,624	3,892,758
Fees, fines and charges for services	4,092,408	-	-	-	-	-	4,092,408
Interest	176,652	-	-	37,748	67,772	232,332	514,504
Other	366,661	-	-	-	42,956	12,275	421,892
Total revenues	20,473,142	1,993,532	747,602	1,676,893	844,409	2,892,333	28,627,911
Expenditures:							
Current:							
General government	9,137,935	268,901	-	-	-	46,877	9,453,713
Public works and sanitation	3,090,994	103,604	-	-	21,362	53,117	3,269,077
Public safety	967,128	-	-	-	-	57,271	1,024,399
Culture and recreation	557,394	-	-	-	-	10,680	568,074
Health	2,776,245	-	-	-	-	-	2,776,245
Housing, welfare and community development	1,356,887	710,326	-	-	-	592,706	2,659,919
Education	-	-	746,713	-	-	301,596	1,048,309
Capital outlays	382,345	899,607	889	-	1,043,564	1,878,617	4,205,022
Debt service:							
Principal	-	-	-	391,000	-	-	391,000
Interest	-	-	-	283,078	-	-	283,078
Bond issuance costs	-	-	-	-	-	5,512	5,512
Total expenditures	18,268,928	1,982,438	747,602	674,078	1,064,926	2,946,376	25,684,348
Excess (deficiency) of revenues over expenditures	2,204,214	11,094	-	1,002,815	(220,517)	(54,043)	2,943,563
Other financing sources (uses):							
Proceeds from general obligation bonds	-	-	-	-	-	1,325,000	1,325,000
Payment of PREPA debt	(105,879)	-	-	-	-	-	(105,879)
Transfers in	126,763	-	-	-	-	-	126,763
Transfers out	-	-	-	(37,021)	(19,392)	(70,350)	(126,763)
Total other financing sources (uses)	20,884	-	-	(37,021)	(19,392)	1,254,650	1,219,121
Net change in fund balances	2,225,098	11,094	-	965,794	(239,909)	1,200,607	4,162,684
Fund balances (deficit) at beginning of year, as restated (note U)	13,947,536	(227,765)	-	3,876,715	4,239,192	5,888,909	27,724,587
Fund balances (deficit) at end of year	\$ 16,172,634	\$ (216,671)	\$ -	\$ 4,842,509	\$ 3,999,283	\$ 7,089,516	\$ 31,887,271

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The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

RECONCILIATION OF STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FISCAL YEAR ENDED JUNE 30, 2009

Net change in fund balances-total governmental funds:	\$	4,162,684
Amounts reported for governmental activities in the statement of activities are different because:		
Governmental funds reports capital assets outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense:		
Expenditures for capital assets:	\$ 4,205,022	
Less: current year depreciation	(1,659,012)	2,546,010
Governmental funds only report the proceeds received in the disposal of assets. In the Statement of Activities, a gain or loss is reported for each disposal. Thus, the change in net assets differs from the change in fund balance by the cost of the disposed asset:		
		(69,638)
Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds:		
Intergovernmental subsidy prior years - General Fund	73,219	
Municipal license tax	4,774	
P.R. Department of Labor (Law No. 52 and 82)	10,420	
P.R. Department of Education	175,000	
P.R. Department of Transportation	68,650	
P.R. Electric Power Authority (PREPA) (current year)	169,306	
P.R. Infrastructure Financing Authority	142,264	
P.R. Department of Correction and Rehabilitation	27,760	
Rural Development Corporation	52,732	
Grant from P.R. Department of Family - Pres	83,133	
Christmas Bonus Reimbursement (current year)	186,669	
Sales and use tax- Municipal Development Fund	24,374	
Sales and use tax- Debt Service Fund	16,408	
Federal Grant- Homeland Security	32,210	
Federal Grant-State and Community Highway Safety	20,540	
Federal Grant-Child Care	84,371	
Federal Grant-CDBG	162,882	
Charges for services	15,483	
Construction permits	38,194	
Interest	2,250	
Donated capital assets	91,133	1,481,772
Revenues reported in funds which are not reported as revenues in the Statement of Activities:		
Property taxes-General Fund (current year)	49,056	
Property taxes-General Fund (prior year)	13,352	
Sales and use tax- Municipal Development Fund (prior year)	36,180	
P.R. Department of Education (prior year)	140,000	
P.R. Department of Labor (Law No. 52 and 82)	17,383	
Rural Development Corporation	165,453	
Grant from P.R. Department of Transportation	61,550	
P.R. Electric Power Authority (PREPA) (prior year)	105,879	
Charges for services	39,603	
Interest (prior year)	8,117	
Federal Grant-HOME	118,788	
Federal Grant-CDBG	173,976	
Federal Grant-State and Community Highway Safety	21,681	
Federal Grant- Homeland Security	40,745	
OCAM - Public Order Code (prior year)	30,674	
Christmas Bonus Reimbursement (prior year)	167,680	(1,190,117)
Proceeds from general obligation bonds are other financing sources in the governmental funds, but an increase of long-term liabilities in the Statement of Net Assets:		
		(1,325,000)
Expenditures reported in funds which are not reported as expenses in the Statement of Activities:		
Matured bonds principal payments-Debt Service Fund (net change)		165,000
Repayment of long-term debt is an expenditure in the governmental funds, but reduces long-term liabilities in the Statement of Net Assets:		
General obligation bonds and notes	226,000	
Other long-term liabilities	874,633	1,100,633
Governmental funds report the effect of bond issuance costs as expenditure when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities. This amount is the net effect of these differences:		
Bond issuance costs	5,512	
Amortization of bond issuance costs	(3,199)	2,313
Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds:		
Compensated absences	(147,091)	
Municipal solid waste landfill (net change)	329,964	
Judgment and legal claims (net change)	147,000	
Christmas bonus	(401,898)	
P.R. Electric Power Authority (PREPA)	(169,306)	
Accrued interest (net change)	1,095	(240,236)
Change in net assets of governmental activities:	\$	6,633,421

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Isabela was founded in 1819. The Municipality is governed by the executive and the legislative branch elected for a four year term during the general elections in Puerto Rico. The Mayor is the executive officer and the legislative branch consists of fourteen (14) members of the Municipal Legislature. The Municipality engages in a comprehensive range of services to the community such as: general government administration, public works, health, environmental control, education, public security, welfare, housing, community development and culture and recreation activities.

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

1. *Financial reporting entity*

The financial reporting entity included in this report consists of the financial statements of the Municipality of Isabela (primary government). To fairly present the financial position and the results of operations of the financial reporting entity, management must determine whether its reporting entity consists of only the legal entity known as the primary government or one or more organizations called component units. The inclusion of a potential component unit in the primary government's reporting entity depends on whether the primary government is financially accountable for the potential component unit or on whether the nature and significance of the relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. There are two methods of presentation of the component unit in the financial statements: (a) blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and (b) discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

The basic criteria for deciding financial accountability are any one of the following:

- a. Fiscal dependency of the potential component unit on the primary government, or
- b. The primary government appoints a voting majority of the potential component unit's governing body and,
 - 1) The primary government can impose its will on the potential component unit and/or,
 - 2) A financial benefit/ burden exists between the primary government and the potential component unit.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

In addition, a legally separate, tax-exempt organization should be discretely presented as a component unit of a reporting entity if *all* of the following criteria are met:

- a. The economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents.
- b. The primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization.
- c. The economic resources received or held by an *individual organization* that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government.

Other organizations should be evaluated as potential component units if they are closely related to, or financially integrated with, the primary government. Professional judgment is applied in determining whether the relationship between a primary government and other organizations for which the primary government is not accountable and that do not meet these criteria is such that exclusion of the organization would render the financial statements of the reporting entity misleading or incomplete.

Based on the above criteria there are no potential component units which should be included as part of the financial statements.

2. *Basis of presentation, measurement focus and basis of accounting*

The financial report of the Municipality consists of the Management Discussion and Analysis (MD&A), the basic financial statements, notes to the financial statements and required supplementary information other than the MD&A. Following is a summary presentation of each, including the measurement focus and basis of accounting. Measurement focus is a term used to describe *which* transactions are recorded within the various financial statements. Basis of accounting refers to *when* transactions are recorded regardless of the measurement focus:

Management Discussion and Analysis

This consists of a narrative introduction and analytical overview of the Municipality's financial activities. This analysis is similar to analysis the private sector provides in their annual reports.

Basic financial statements

The basic financial statements include both government-wide and fund financial statements. Both levels of statements categorize primary activities as governmental type, which are primarily supported by taxes and intergovernmental revenues.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Government-wide statements

The government-wide statements consist of a Statement of Net Assets and a Statement of Activities. These statements are prepared using the economic resources measurement focus, which concentrates on an entity or fund's net assets. All transactions and events that affect the total economic resources (net assets) during the period are reported. The statements are reported on the accrual basis of accounting. Revenues are recognized in the period earned and expenses recognized in the period in which the associated liability is incurred. Fiduciary activities, if any, whose resources are not available to finance government programs, are excluded from the government-wide statements. The effect of inter-fund activities is eliminated.

The Statement of Net Assets incorporates all capital (long lived) assets and receivables as well as long term debt and obligations. The Statement of Activities reports revenues and expenses in a format that focus on the net cost of each function of the Municipality. Both the gross and net cost of the function, which is otherwise being supported by the general government revenues, is compared to the revenues generated directly by the function. This Statement reduces gross expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. Program revenues must be directly associated with the function.

The types of transactions included as program revenues are: charges for services, fees, licenses and permits; operating grants which include operating-specific and discretionary (either operating or capital) grants; and capital grants which are capital-specific grants. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes. Property taxes (imposed nonexchange transactions) are recognized as revenues in the year for which they are levied and municipal license taxes and sales and use taxes (derived tax revenues) when the underlying exchange has occurred. Revenues on both operating and capital grants are recognized when all eligibility requirements (which include time requirements) imposed by the provider have been met. For certain expenditure-driven grants, revenue is recognized after allowable expenditures are incurred. As a policy, indirect expenses in the Statement of Activities are not allocated. The Municipality first uses restricted assets for expenses incurred for which both restricted and unrestricted assets are available.

The Municipality reports deferred revenues in the government-wide statements. Deferred revenues arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed and the revenue is recognized.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The Municipality has elected not to follow subsequent statements and interpretations issued by the FASB after November 30, 1989.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Fund Statements

The financial transactions of the Municipality are recorded in individual funds, each of which are considered an independent fiscal entity. Each fund is accounted for by providing a separate set of self balancing accounts that comprise its assets, liabilities, reserves, fund equity, revenues and expenditures. Funds are segregated according to their intended purpose which helps management in demonstrating compliance with legal, financial and contractual provisions. Governmental Funds are those through which most governmental functions of the Municipality are financed. The governmental fund statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances with one column for the general fund, one for each major fund and one column combining all non-major governmental funds. Major funds are determined based on a minimum criterion, that is, a percentage of the assets, liabilities, revenues or expenditures or based on the Municipality's official's criteria if the fund is particularly important to financial statement users (for Community Development Block Grant and Head Start Program Funds).

The Municipality reports the following major governmental funds:

General Fund: This is the operating fund of the Municipality and accounts for all financial resources, except those required to be accounted for in another fund.

Community Development Block Grant Program Fund (CDBG): CDBG fund is used to account for revenues sources for the development of viable urban communities by providing decent housing, a suitable living environment and expanding economic opportunities, principally for persons of low and moderate income.

Head Start Program Fund: Head Start fund is used to account for revenues sources for the related activities that promote school readiness by enhancing the social and cognitive development of low-income children through the provisions of comprehensive health, educational, nutritional, social and other services.

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

Commonwealth Legislature Resolutions Fund: The Commonwealth Legislative Resolutions Fund is used to account for grants from the Commonwealth's Legislature.

Governmental funds, reported in the fund statements, are accounted for using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method of accounting, revenues are recognized when they are susceptible to accrual (i.e. both measurable and available). Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Municipality considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Revenues susceptible to accrual include property taxes, recognized as revenues in the year for which they are levied; municipal license taxes and sales and use taxes, recognized when the underlying exchange has occurred and time requirements are met, and interest. In applying the susceptible to accrual concept to intergovernmental revenues, revenues are recognized when all eligibility requirements (including time requirements) imposed by the provider have been met and revenue becomes available. There are, however, essentially two types of these revenues. In the first case, on expenditure-driven grants, monies must be expended on the specific project or purpose (eligibility requirement), before any amounts are paid to the Municipality. Revenue is, therefore, recognized as expenditures are incurred to the extent available. In the other cases, monies are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. In these cases revenues are recognized as the time of receipt or earlier if the susceptible to accrual criteria is met. Licenses and permits, charges for services, rent, fines and miscellaneous revenues are generally recorded as revenues when received or are recognized earlier if the susceptible to accrual criteria is met.

The Municipality reports in the governmental funds statements deferred revenues which arise when potential revenue does not meet both measurable and available criteria for recognition in the current period (in the government-wide statements revenue is recognized as soon as it is earned regardless of its availability). Deferred revenues also arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met. (In case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the revenue recognition criteria is 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 the revenue is recognized.

Expenditures are generally recognized when the related liability is incurred. Certain exceptions to this fundamental concept include the following: (1) payments of principal and interest on general long term debt, which are recorded as expenditures when due, except for principal and interest due on July 1 (in this case amounts are recorded as liabilities and expenditures on June 30 since amounts have been accumulated or transferred to the debt service fund before July 1 payments are made) and (2) vested compensated absences, claims and judgments and special termination benefits which are recorded as expenditures only to the extent that they are expected to be liquidated with expendable financial resources (in the government-wide statements the expense and related accrual liability for long- term portions of debt must be included).

Since the governmental fund statements are presented on a different measurement focus and basis of accounting than the government-wide statements, a reconciliation is necessary to explain the adjustments needed to transform the fund financial statements into the government-wide statements. This reconciliation is part of the financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Notes to Financial Statements

The notes to financial statements provide information that is essential to a user's understanding of the basic financial statements.

Required Supplementary Information:

Required supplementary information consists of the Budgetary Comparison Schedule – General Fund as required by GASB.

3. *Cash and investments and restricted cash with fiscal agents*

Cash consist of cash on hand, demand deposits and short term investments with original maturities of three months or less from the date of acquisition. Investments consist of nonnegotiable certificates of deposits with original maturity of more than three months. The Municipality follows the practice of pooling cash of all funds except for certain Commonwealth's grants, restricted funds generally held by outside custodians and federal grants. Available pooled cash balance beyond immediate needs is invested in certificates of deposits. Cash and investments related to Commonwealth and Federal grants are restricted since their use is limited by applicable agreements or required by law.

Restricted cash with fiscal agent in the debt service fund consists of the undisbursed balance of property and sales tax collections retained by the Commonwealth of Puerto Rico which are restricted for the repayment of the Municipality's general and special obligation bonds and notes as established by law. Restricted cash with fiscal agent of the other governmental funds represent the undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by the GDB or a federal government agency.

4. *Receivables and due from governmental entities*

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions.

Amounts due from federal government represent amounts owed to the Municipality for the reimbursement of expenditures incurred pursuant to federally funded programs. Amounts reported in the debt service fund represent property and sales tax revenues of current fiscal year collected by the CRIM (property tax) and the Puerto Rico Department of Treasury (sales tax) on the subsequent fiscal year.

5. *Interfund receivables and payables*

Activities among funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due from/to other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances among the funds are reported as "due from/to other funds".

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

6. *Inventories*

The Municipality purchases gasoline, oil and other expendable supplies held for consumption. The cost of those purchases is recorded as expenditure when incurred in the appropriate fund but the year-end inventory is not recorded in the Statement of Net Assets, as management believes is not significant. Only inventory of medicines and medical supplies of the Municipality's Advanced Medical Center ("CIMA") in the amount of \$203,557 are included in the financial statements.

7. *Capital assets*

Capital assets of the primary government, which include property, equipment, and infrastructure, (e.g., roads, bridges, sidewalks, and similar items) are reported in the governmental activities column in the Statement of Net Assets. Capital assets are capitalized at historical cost or estimated historical cost if historical cost is not available. Donated assets are recorded as capital assets at their estimated fair market value at the date of donation. The Municipality maintains a threshold level of \$500 or more for capitalizing vehicles, machinery and equipment. Infrastructure assets are capitalized based on a percentage of the estimated useful life. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

All capital assets, other than land and construction in progress, are depreciated using the straight-line method over the following useful lives:

<u>Description</u>	<u>Years</u>
Land improvements	50
Buildings and building improvements	50
Leasehold improvements	Lease term
Infrastructure	10-50
Vehicles, machinery and equipment	5-10

In accordance with current accounting standards capital assets are reviewed for impairment. Impairment occurs when there is a significant decline in asset service utility due to the occurrence of a prominent event or change in circumstances affecting the asset. Current standards provide guidance for accounting and reporting for impairment and for insurance recoveries.

8. *Long-term obligations*

Long-term debt and other long-term obligations, which are reported as liabilities in the governmental activities column in the Statement of Net Assets, consist of general and special obligation bonds, liabilities for compensated absences, claims and judgments, and long-term liabilities to other governmental entities.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

9. *Deferred bond issuance costs*

Bond issuance costs are reported as deferred charges and amortized as required by current standards. Governmental fund types recognize bond issuance costs as expenditures during the current period. Those issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the appropriate fund.

10. *Compensated absences*

The Municipality's employees accumulate vacation, sick leave and compensatory time based on continuous service. Compensated absences are recorded as a liability if (1) are earned on the basis of services already performed by employees, (2) it is probable that will be paid (in the form of paid time off, cash payments at termination or retirement, or some other means) and (3) are not contingent on a specific event (such as illness).

The compensated absences are accumulated on the basis of 2½ days per month of vacation and 1½ days per month of sick pay and compensatory time up to a maximum of 60 days of vacations and 90 days of sick leave. Upon separation from employment the accumulated vacations are liquidated up to the maximum number of days. Accumulated sick leave, which is accrued based on all vesting amounts for which payment is probable, is liquidated to employees with 10 years or more service up to the maximum number of days.

The accrual of compensated absences includes estimated payments that are related to payroll. The entire compensated absence liability is reported on the government-wide financial statements. For governmental fund financial statements, the current portion of unpaid compensated absences is the amount that is normally expected to be paid using expendable available financial resources. The non-current portion of the liability is not reported.

Pursuant to Law No. 152 of August 20, 1996 effective July 1, 1997 the Municipality is required to pay any excess of vacations and sick leave accumulated over 90 days as of December 31 of each year. Payments should be made on or before March 31 of the following year.

11. *Fund balances and Net Assets*

a. Fund balances:

In the fund financial statements, governmental funds report reserved and unreserved fund balances. Reservations of fund balances represent portions that are legally segregated for a specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balances:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Encumbrances:	Represent future expenditures under purchase orders and other commitments, which generally will become liabilities in future periods as the goods or services are received.
Inventories	Represent the valuation amount assigned for the restriction and use of resources accounted in inventory on hand.
Debt Service:	Represent net assets available to finance future debt service payments.
Capital Projects:	Represent amounts to be used for future expenditures for capital projects under contracts and other commitments. These commitments generally will become liabilities in future periods as the projects are completed.
Other specified purposes:	Represent amounts to be used for future expenditures of Federal and Commonwealth's grants as well as funds reserved through enabling legislation passed by the government itself, to be used to finance activities other than construction or capital improvement commitments.
Advances:	Represent the non-current portion of interfund loans.

Fund balance unreserved-designated represents amounts that Management has identified for future spending and not legally segregated.

b. Net assets

In the government-wide statements net assets are segregated into three categories:

Invested in capital assets, net of related debt:	Consist of capital asset balances net of accumulated depreciation and outstanding balances of any bonds, notes and other borrowings that are attributable to the acquisition, construction, or improvement of those assets. This category should not include cash that is restricted to capital asset acquisition or construction (unspent bond proceeds) and any unamortized debt issue costs.
Restricted net assets:	Represent net assets (restricted assets net of related debt) that are subject to restrictions beyond the Municipality's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation (including enabling legislation passed by the government itself).
Unrestricted net assets:	Represent net assets that do not meet the definition of net assets invested in capital assets, net of related debt or restricted. Unrestricted assets are often designated to indicate that management does not consider them to be available for general operations. These types of constraints are internal and management can remove or modify them. Designations are not reported on the face of the statement of net assets.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE B – CUSTODIAL CREDIT RISK - DEPOSITS

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The Municipality maintains cash deposits in commercial and governmental banks located in Puerto Rico.

Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal deposit insurance. All securities pledged as collateral by the Municipality are held by the Secretary of Treasury of Puerto Rico in the Municipality's name. At year-end the Municipality's bank balance in commercial banks amounts to \$24,064,209. Deposits in governmental banks (all of which are uninsured and uncollateralized), are exposed to custodial credit risk. At year-end the Municipality's bank balance in governmental banks amounts to \$6,879,417.

NOTE C – INVESTMENT HELD WITH FISCAL AGENT

The investment held with fiscal agent consists of a non-participating investment contract (non-rated guaranteed investment contract, "GIC"). This represents the investment of the undisbursed proceeds of the \$3,010,000 general obligation bond under custody of GDB, the Municipality's fiscal agent, pursuant to the bond purchase agreement. The GIC, with an outstanding balance of \$756,822 as of June 30, 2009 earns interest at a variable rate (LIBOR minus .125%, 1.42440% as of June 30, 2009) and matures on November 2, 2009. GIC outstanding balance is valued at cost.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico. Accordingly, the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults on the Municipality's investments are considered low at June 30, 2009.

NOTE D – RECEIVABLES

Accounts receivable – other as of June 30, 2009 follows:

	<u>Amount</u>
Construction permits	\$ 140,064
Healthcare providers billings	89,557
Interest	57,300
	<hr/>
	\$ 286,921

Certain amounts receivable are recorded as deferred revenue in the governmental funds statements since they are not available as required by current standards. See related note H.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE E – DUE FROM (TO) GOVERNMENTAL ENTITIES

1. Amounts due from governmental entities as of June 30, 2009 follows:

	<u>Commonwealth Government</u>	<u>Federal Government</u>
Municipal Revenue Collection Center (CRIM) – intergovernmental subsidy (general fund) – prior years	\$ 73,219	\$ -
P.R. Electric Power Authority (PREPA)	275,186	
P.R. Department of Treasury - Christmas bonus reimbursement	186,669	-
P.R. Department of Education	210,000	-
Municipal Revenue Collection Center (CRIM) – property taxes (debt service fund)	228,763	-
P.R. Department of Health	100,240	-
P.R. Department of Labor-Law No. 52	12,279	-
P.R. Department of Labor-Law No. 82	15,727	-
P.R. Department of Transportation	293,428	-
Rural Development Corporation	131,165	-
Office of Commissioner of Municipal Affairs – Commonwealth Legislature Resolutions	291,332	-
P.R. Department of Family – Pres	83,133	-
Office of Commissioner of Municipal Affairs – CDBG	-	70,806
U.S. Department of Housing and Urban Development – CDBG	-	455,410
U.S. Department of Health and Human Services – Head Start	-	149,070
P.R. Department of Family – Child Care	-	462,466
P.R. Traffic Safety Commission	-	20,540
Others	47,606	32,386
	<u>\$ 1,948,747</u>	<u>\$ 1,190,678</u>

See note H for detail of amounts due from governmental entities recorded as deferred revenue.

2. Amounts due to governmental entities as of June 30, 2009 follows:

	<u>Commonwealth Government</u>
P.R. Employees Retirement System (current debt)	\$ 92,742
P.R. Department of Labor - unemployment	21,862
P.R. Aqueduct and Sewer Authority (PRASA)	12,435
	<u>\$ 127,039</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE F - INTERFUND TRANSACTIONS

1. Due from/to other funds:

Amounts due from/to other funds represent advances to other funds for payroll and payroll taxes expenditures, as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General Fund	Major funds:	
	CDBG	\$ 57,833
	Head Start	129,512
	Other governmental funds:	
	Public Order Code	303,298
	Child Care	465,973
	TANF	175,712
	Traffic Safety Commission	179,584
	Section 8 HCV	98,180
	Rural Development Corporation	131,537
	Office of Public Safety Affairs	40,745
	P.R. Dept. of Transportation	192,117
	P.R. Dept. of Family - Pres	83,133
	Others	36,197
		<u>\$ 1,893,821</u>
Commonwealth		
Legislative Resolutions:	Other governmental funds:	
	"BGF Parque Lineal Pasivo"	<u>\$ 33,545</u>
Other governmental funds:	Major funds:	
WIA	General Fund	<u>\$ 9,068</u>

2. Advances to(from) other funds:

Advances to (from) other funds in the amount of \$1,307,497 represent long-term advances by the Commonwealth Legislature Resolutions Fund to the General Fund in previous years to cover operational expenditures.

3. Transfers in (out):

Transfers among individual funds were made for operational purposes. Transfers include (1) interest earned on restricted cash with fiscal agent in the debt service fund and operating and capital improvement loans in other governmental funds which are transferred to the general fund, (2) interest in Commonwealth Legislature Resolutions funds which is transferred to the general fund and, (3) principal and interest payments of long-term debt transferred from the general fund to the debt service fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE G – CAPITAL ASSETS

Capital assets and depreciation activity as of and for the year ended June 30, 2009 is as follows:

	Balance July 1, 2008 as restated	Increases	Decreases	Balance June 30, 2009
<u>Governmental activities:</u>				
Capital assets, not being depreciated:				
Land	\$ 4,055,589	\$ 71,800	\$ -	\$ 4,127,389
Construction in progress	5,823,626	3,049,186	3,282,984	5,589,828
Total capital assets not being depreciated:	9,879,215	3,120,986	3,282,984	9,717,217
Capital assets, being depreciated:				
Land improvements	14,650	-	-	14,650
Buildings and building improvements	16,394,854	2,949,640	-	19,344,494
Leasehold improvements	505,233	-	-	505,233
Infrastructure	12,673,899	1,068,120	149,895	13,592,124
Vehicles, machinery and equipment	8,291,573	315,041	55,855	8,550,759
Total capital assets being depreciated	37,880,209	4,332,801	205,750	42,007,260
Less accumulated depreciation for:				
Land improvements	171	293	-	464
Buildings and building improvements	2,553,066	666,320	-	3,219,386
Leasehold improvements	121,714	37,892	-	159,606
Infrastructure	1,817,463	238,326	116,008	1,939,781
Vehicles, machinery and equipment	3,495,738	716,181	24,592	4,187,327
Total accumulated depreciation	7,988,152	1,659,012	140,600	9,506,564
Total capital assets being depreciated, net	29,892,057	2,673,789	65,150	32,500,696
Governmental activities capital assets, net	<u>\$ 39,771,272</u>	<u>\$ 5,794,775</u>	<u>\$ 3,348,134</u>	<u>\$ 42,217,913</u>

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

Governmental activities:

General government	\$ 37,381
Public works and sanitation	654,571
Public safety	99,884
Culture and recreation	647,839
Health	27,333
Welfare and community development	55,477
Education	136,527
Total depreciation expense, governmental activities	<u>\$ 1,659,012</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE H – DEFERRED REVENUES – GOVERNMENTAL FUNDS

Deferred revenues - Commonwealth Government and Other represent revenues not available as required by current standards and for Federal Grants represent resources received before allowable expenditures are incurred or not available as required by current standards. A detail of these balances follows:

	Commonwealth Government	Federal Grants	Other
<u>Major fund - general fund:</u>			
Municipal Revenue Collection Center (CRIM) - intergovernmental subsidy prior years (general fund)	\$ 73,219	\$ -	\$ -
P.R. Department of Treasury - Christmas bonus reimbursement	186,669	-	-
P.R. Department of Education	175,000	-	-
P.R. Department of Health	14,320	-	-
P.R. Department of Labor - Law No. 52	11,332	-	-
P.R. Department of Labor - Law No. 82	10,420	-	-
P.R. Electric Power Authority (PREPA)	275,186	-	-
Others	54,596	-	-
Construction permits	-	-	140,064
Healthcare providers billings	-	-	33,216
<u>Major fund - Community Development Block Grant fund:</u>			
Office of Commissioner of Municipal Affairs -CDBG	-	32,557	-
U.S. Department of Housing and Urban Development - CDBG	-	185,609	-
<u>Major fund - Commonwealth Legislature resolutions fund:</u>			
Commonwealth Legislative Resolutions	142,264	-	1,347
<u>Other governmental funds:</u>			
P.R. Department of Transportation	272,597	-	-
Rural Development Corporation	55,097	-	-
P.R. Department of Family - Pres	83,133	-	-
P.R. Department of Family - Child Care	-	226,278	-
Office of Public Safety Affairs	-	32,210	-
P.R. Traffic Safety Commission	-	20,540	-
Others	-	-	903
	<u>\$ 1,353,833</u>	<u>\$ 497,194</u>	<u>\$ 175,530</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT

1. Summary of long-term debt activity

The following summarizes activity in long-term debt for the fiscal year ended June 30, 2009:

	<u>Balance at July 1, 2008</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance at June 30, 2009</u>	<u>Due within one year</u>
General, Special Obligations Bonds and Notes	\$ 7,680,024	\$ 1,325,000	\$ 226,000	\$ 8,779,024	\$ 392,000
Note payable to CRIM-LIMS	217,123	-	57,559	159,564	61,034
Note payable to CRIM –Financing of delinquent accounts	69,128	-	2,880	66,248	2,880
Note payable to PR Department of Labor	59,619	-	59,619	-	-
Note payable to P.R. Solid Waste Authority	134,905	-	36,360	98,545	37,419
Note Payable to P.R. Treasury Department	458,778	-	145,362	313,416	152,799
Note payable to ERS	114,554	-	55,444	59,110	59,110
Note payable – Section 108 Loan Guarantee	1,200,000	-	-	1,200,000	269,000
Landfill Obligation	4,649,489	261,789	591,753	4,319,525	-
Compensated absences	2,545,681	366,123	219,032	2,692,772	194,267
Christmas bonus	361,016	401,898	361,016	401,898	401,898
Claims and judgments	150,000	3,000	150,000	3,000	-
Payable to CRIM- excess of property tax advances over actual collections	50,514	49,056	50,514	49,056	-
Payable to PREPA	211,759	169,306	105,879	275,186	105,880
	<u>\$ 17,902,590</u>	<u>\$ 2,576,172</u>	<u>\$ 2,061,418</u>	<u>\$ 18,417,344</u>	<u>\$ 1,676,287</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

2. General and special obligation bonds and notes

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2009 amount to \$8,779,024. All these bonds are serviced by the Governmental Development Bank of Puerto Rico (GDB) maturing at various dates. As required by law, the Commonwealth Government is obligated to collect property taxes for payment of principal and interest on bonds and notes. In addition, .2% of the .5% municipal sales and use tax collected by the P.R. Department of Treasury is deposited in a "Municipal Redemption Fund" to finance loans to Municipalities subject to restrictions imposed by law. Debt service funds has been established for the bonds and notes at GDB with the proceeds of those property and sales and use taxes, whereby sufficient funds must be set aside in order to cover the projected debt service requirement, before any new bonds are issued.

A detail of the general and special obligation bonds and notes as of June 30, 2009 follows:

	Outstanding Amount
1996 general obligation bonds of \$525,000 due in annual installments ranging from \$13,000 to \$36,000 through January 1, 2021; bearing interest at 4.50%	\$ 339,000
1999 general obligation bonds of \$410,000 due in annual installments ranging from \$11,000 to \$29,000 through January 1, 2024; bearing interest at 4.50%	320,024
2000 general obligation bonds of \$305,000 due in annual installments ranging from \$20,000 to \$40,000 through July 1, 2010; bearing interest at rates ranging from 2.70% to 7.81% (4.10% at June 30, 2009)	80,000
2001 general obligation bonds of \$3,455,000 due in annual installments ranging from \$45,000 to \$290,000 through July 1, 2026; bearing interest rates ranging from 5.00% to 7.50% (5.15% at June 30, 2009)	3,005,000
2006 general obligation bonds of \$255,000 due in annual installments ranging from \$5,000 to \$25,000 through July 1, 2029; bearing interest rates ranging from 4.37% to 5.31% (4.38% at June 30, 2009)	235,000
2006 general obligation bonds of \$600,000 due in annual installments ranging from \$25,000 to \$60,000 through July 1, 2021; bearing interest rates ranging from 6.60% to 7.25% (5.40% at June 30, 2009)	550,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2008

NOTE I – LONG-TERM DEBT – Continued

	<u>Outstanding Amount</u>
2006 general obligation bonds of \$3,010,000 due in annual installments ranging from \$40,000 to \$260,000 through July 1, 2031; bearing interest rates ranging from 5.69% to 6.75% (4.47% at June 30, 2009)	2,925,000
2008 general obligation note of \$1,325,000 due in annual installments ranging from \$150,000 to \$240,000 through July 1, 2015; bearing interest rates ranging from 1.53% to 7.50% (5.40% at June 30, 2009)	<u>1,325,000</u>
	<u><u>\$ 8,779,024</u></u>

The annual requirement to amortize general and special obligation bonds and notes as of June 30, 2009 follows:

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2010	\$ 392,000	\$ 544,657
2011	419,000	550,263
2012	406,000	521,498
2013	438,000	490,449
2014	474,000	457,017
2015-2019	2,109,000	1,826,489
2020-2024	2,041,024	1,142,984
2025-2029	1,755,000	426,810
2030-2032	745,000	47,204
Totals	<u>\$ 8,779,024</u>	<u>\$ 6,007,371</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

3. Other long-term liabilities

Outstanding
Amount

Note payable to CRIM (LIMS) – On June 27, 2001 the Municipality entered into a financing agreement with the CRIM in the amount of \$519,187 for the payment of the Municipality's share of the cost of a management information system (LIMS) acquired by the CRIM for the management of taxpayer's properties located in Puerto Rico. The note is payable in semiannual installments of \$34,817, including interest of 5.95% and is due on November 28, 2011. Amount is repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center (CRIM). Debt service requirements in future years are as follows:

\$ 159,564

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2010	\$ 61,034	\$ 8,599
2011	64,719	4,914
2012	33,811	1,006
Totals	<u>\$ 159,564</u>	<u>\$ 14,519</u>

Note payable to CRIM (Financing of delinquent accounts)– On April 2, 2002, the Municipality entered into a financing agreement with the CRIM in the amount of \$471,041, to finance delinquent property tax accounts sold to private investors, under the provision of Law No. 146 of October 11, 2001. The agreement is in the form of a non-revolving line of credit bearing interest of 6.5% for the first five years and variable for the next 25 years at 125 points over London Interbank Offered Rate (LIBOR) and is due on December 1, 2032. As described in Law No. 146, interest payments for the first five years were financed through .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico's general fund. Also, during the first five years any collection from those delinquent accounts was credited to the loan principal. After the five-year period the loan outstanding balance was restructured for a 25-year period. Amount is repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center (CRIM). Debt service requirements in future years are as follows:

\$ 66,248

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2010	\$ 2,880	\$ 4,075
2011	2,880	3,897
2012	2,880	3,717
2013	2,880	3,538
2014	2,880	3,359
2015-2019	14,402	14,108
2020-2024	14,402	9,630
2025-2029	14,402	5,151
2030-2032	8,642	941
Totals	<u>\$ 66,248</u>	<u>\$ 48,416</u>

Note payable to Puerto Rico Solid Waste Authority – On September 17, 2004, the Municipality entered into a financing agreement with the PR Solid Waste Authority for a total amount of \$307,944 for unpaid operating lease charges related to equipment used in the Municipality's landfill. The agreement is in the form of a non-interest bearing note (imputed interest of 6%) payable in semiannual installments of \$20,000, and a final payment of \$22,944 on January 1, 2012. The note balance as of June 30, 2009 is net of an unamortized discount of \$4,399 and is being paid from unrestricted funds. Debt service requirements in future years are as follows:

\$ 98,545

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2010	\$ 37,419	\$ 2,581
2011	38,509	1,491
2012	22,617	327
Totals	<u>\$ 98,545</u>	<u>\$ 4,399</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

Note Payable–Puerto Rico Treasury Department- On February 16, 2007 the Municipality settled a legal case for \$825,000 and refinanced this debt on a long-term basis through a \$728,622 non-interest bearing note (imputed interest rate is 5.00%), from the Puerto Rico Department of the Treasury. The note is payable in monthly installments of \$13,750 (including interest) through June 30, 2011. The note balance as of June 30, 2009 is net of an unamortized discount of \$16,584 and will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM). Debt service requirements in future years are as follows:

\$ 313,416

June 30,	Principal	Interest
2010	\$ 152,799	\$ 12,201
2011	160,617	4,383
Totals	\$ 313,416	\$ 16,584

Note payable to Employee’s Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS).

– On June 29, 2007 the Board of Trustees of the Employee’s Retirement System of the Government of Puerto Rico an its Instrumentalities (ERS) approved Resolution No. 2007-02 authorizing the ERS to establish payment plans with employers related to the application of certain “Special Laws” issued by the Commonwealth Government. Those Special Laws granted increases in pensions to retired employees of the Municipality. This obligation was recognized by the Municipality prior to June 30, 2007. On November 30, 2007 the Municipality refinanced this debt on a long term basis through a \$201,060 non-interest bearing note with the ERS. The note has an imputed interest rate is 6.48% and was recorded at its present value of \$195,732 net of an unamortized discount of \$14,328. The note is payable in annual installments of \$63,018 (including interest, is due on February 26, 2010 and will be repaid with unrestricted funds. Debt service requirements in future years are as follows:

\$ 59,110

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

June 30,	Principal	Interest
2010	\$ 59,110	\$ 3,908

Note payable Section 108 Loan Guarantee – The Municipality entered into a financing agreement with the US Department of Housing and Urban Development (HUD) through a contract for Loan Guarantee Assistance under Section 108 of the Housing and Community Act of 1974, as amended. The agreement, for a maximum commitment of \$4,850,000 will finance the construction of a Youth Sports and Education Center. On October 1, 2007 the Municipality received \$1,200,000 on advance funds under a \$1,345,000 variable/fixed rate note dated July 12, 2007, bearing interest at LIBOR + .20% and due on August 1, 2013. The VRF Note is designed to convert to a fixed rate note on its Conversion Date. The following Commitment Schedule to the Note represents the agreed-upon repayment schedule referred to in the Section 108 commitment against which the Municipality requests advances when funds are needed. The schedule of principal and interest to the fixed rate Note will be filed out as of the Conversion Date based on the cumulative amount of advances per principal due date that the Municipality has received on or before such date. The Note will be repaid from appropriation of funds from the Community Development Block Grant Program (Entitlement). Interest payments on fiscal year 2008-2009 amounts to \$31,244. Debt service requirements in future years are as follows:

\$ 1,200,000

June 30,	Principal
2010	\$ 269,000
2011	269,000
2012	269,000
2013	269,000
2014	124,000
Totals	\$ 1,200,000

Subsequent to June 30 (August 20, 2009) the Municipality received \$3,650,000 representing the remaining advance funds under a \$4,850,000 variable/fixed rate note dated June 29, 2009 bearing interest at LIBOR + .20% and due on August 1, 2026. The \$4,850,000 represents the maximum commitment amount under contract. The VRF Note is designed to convert to a fixed rate note on its Conversion Date.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

Landfill obligation – represents the outstanding balance of the estimated liability for landfill closure and post-closure care costs, based on a 90% usage of the landfill. The total estimate for these costs amounts to \$4,800,000 as of June 30, 2009.	\$ 4,319,525
Compensated absences – includes accrued vacations, sick leave benefits and other benefits with similar characteristics such as compensatory time, represents the Municipality's commitment to fund such costs from future operations. Amount is repaid with unrestricted funds.	\$ 2,692,772
Christmas Bonus – represents the accrued portion corresponding to fiscal year 2008-2009 of the Christmas bonus to be paid in December 2009.	\$ 401,898
Claims and judgments - represents amounts accrued arising from a final settlement of one case to be paid subsequently with unrestricted funds by the Municipality.	\$ 3,000
Payable to CRIM – represents the balance owed to CRIM at June 30, 2009 for excess of advances of property tax and other subsidies over preliminary amount of property tax collections for the fiscal year ended 2009. This amount will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund sent to the Municipality by the Municipal Revenue Collection Center (CRIM).	\$ 49,056
Payable to PREPA - As required by Act No. 83 of May 2, 1941 the Puerto Rico Electric Power Authority ("PREPA") should annually pay to the Municipalities of Puerto Rico a contribution in lieu of tax ("CELI") based on certain requirements as specified by the mentioned Act. The amount of CELI obligation is used by the Municipalities to finance the annual electric utility expense payment to PREPA. For fiscal year 2006-2007 the Municipality's annual energy charges amounts to \$1,480,096 but the CELI obligation determined by PREPA amounted to \$1,162,458. As communicated by PREPA the excess amount of \$317,638 was recorded as a payable to the Municipality and will be amortized over a three-year period against the corresponding receivable for the same amount. As of June 30, 2009 the outstanding amount of \$ 105,880 is recognized by the Municipality as a receivable and a liability to PREPA. For fiscal year 2007-2008 the Municipality's annual energy charges amounts to \$1,788,230 but the CELI obligation amounted to \$1,618,924. The excess amount of \$169,306 was also recorded as a payable and a receivable for the same amount. No amortization period was established by PREPA. Debt service requirements in future years are as follows:	\$ 275,186

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE I – LONG-TERM DEBT – Continued

<u>June 30</u>	<u>Principal</u>
2010	\$ 105,880
2011-2015	169,306
Totals	<u>\$ 275,186</u>

NOTE J – LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS OBLIGATIONS

Commonwealth and Federal laws and regulations require the Municipality to place a final cover on its landfill when it stops accepting waste and perform certain maintenance and monitoring functions at the landfill site for thirty years after closure. In addition to the operating expenditures related to current activities of the landfill, an expense provision and related liability are being recognized based on future closure and post-closure care costs that will be incurred near or after the date the landfill no longer accepts waste. The Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations. As a result of this study, the Municipality has recognized an estimated liability for future closure and post-closure care costs.

The recognition of this liability is based on the amount of the landfill used during the year. The estimated liability for landfill closure and post-closure care costs has an outstanding balance of \$4,319,525 as of June 30, 2009, which is based on a 90% usage of the landfill. It is estimated that an additional \$480,475 will be recognized as closure and post-closure care expenditures between the balance sheet date and the date the landfill is expected to be filled to capacity (April 2011). The estimated total current costs of the landfill closure and post-closure care (\$4,800,000) is based on the amount that would be paid if all the equipment, facilities and services required to close, monitor and maintain the landfill were acquired as of June 30, 2009. However, the actual cost of closure and post-closure care may be higher due to inflation, changes in technology, or changes in landfill laws and regulations. As of June 30, 2009, the Municipality has not made contributions to finance closure and post-closure care costs.

NOTE K – PROPERTY TAXES

The Municipal Revenue Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible for the assessment, collection and distribution of real and personal property taxes. The tax on personal property is self-assessed by the taxpayer. The assessment is made on a return, which must be filed with the CRIM by May 15 of each year and is based on the current value at the date of the assessment. Real property is assessed by the CRIM. The tax is general assessed on January 1 on all taxable property located within the Municipality and is based on the current value existing in the year 1957. For personal property the tax is due with the return filed on or before May 15. Taxes on real property may be paid on two equal installments, July 1st and January 1st. Total tax rates in force as of June 30, 2009 are 7.03% for personal property and 9.03% for real property. The distribution of these rates follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE K – PROPERTY TAXES – Continued

<u>Description</u>	<u>Personal Property</u>	<u>Real Property</u>
Basic property tax rate, which is appropriated for general purposes and accounted in the Municipality's general fund:	4.00%	6.00%
Percent that belongs to the Commonwealth's debt service fund:	1.03%	1.03%
Percent that belongs to the Municipality's debt service fund:	<u>2.00%</u>	<u>2.00%</u>
Total tax rate:	7.03%	9.03%
Discount granted by law to the taxpayers but reimbursed to the Municipality by the P.R. Treasury Department:	<u>(.20%)</u>	<u>(.20%)</u>
Total percent to be paid by taxpayers:	<u><u>6.83%</u></u>	<u><u>8.83%</u></u>

Residential real property occupied by its owner is exempt by law from property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the Puerto Rico Department of Treasury assumes payment of the basic tax to the Municipality, except for residential units assessed at less than \$3,500 on which a complete exemption is granted. Revenue related to exempt property is recorded in the General Fund. The Municipality grants a complete exemption from personal property taxes up to an assessment value of \$50,000 to retailers with annual net sales of less than \$150,000.

The CRIM advances funds to the Municipality based on an estimate of special governmental subsidies and the property taxes to be levied and which are collected in subsequent periods. This distribution includes advances of property tax and amounts of municipal equalization fund from the Commonwealth government. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. The CRIM prepares a preliminary settlement not later than three months after fiscal year-end and a final settlement not later than six months after fiscal year-end. If actual collections exceed the advances a receivable from CRIM is recorded. However, if advances exceed actual collections, a payable to CRIM is recorded. For the fiscal year 2008-2009 the CRIM performed the preliminary settlement and determined that that Municipality has a net debt of \$49,056 which is recorded as a long-term debt in the government-wide statement since it will not be paid with expendable available resources as required by current standards.

NOTE L – MUNICIPAL LICENSE TAXES

Municipal License taxes are assessed annually by the Municipality to all organizations or entities subject to the tax doing business in the Municipality's location except for entities totally or partially exempt pursuant to certain Commonwealth's statutes. This tax is based generally on volume of business or gross sales as shown in a tax return that should be submitted on or before April 15. During the fiscal year ended June 30, 2009 the tax rates were as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE L – MUNICIPAL LICENSE TAXES – Continued

Financial business – 1.50% of gross revenues
Other organizations – .50% of gross revenues, except organizations in “Special Development Urban Area” which apply:
 Up to \$100,000 – .30% of gross revenues
 Up to \$200,000 – .40% of gross revenues
 Up to \$200,000 – .50% of gross revenues

The tax is due in two equal installments on July 1 and January 1 of each fiscal year. Tax revenue is recognized at that moment by the Municipality. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year in the amount of \$2,010,302 are recorded as deferred revenues.

NOTE M – SALES AND USE TAXES

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

Section 6189 of the Puerto Rico Internal Revenue Code of 1994, as amended, authorizes the Municipalities in Puerto Rico to impose a sales and use tax to consumers. This tax must be imposed in conformity with the base, exemptions and limitations contained in Subtitle BB of the Code. The municipal sales and use tax is specifically imposed over all sales transactions of taxable items and combined transactions (as defined by the municipal internal regulation) taken place within municipal limits. The municipal sales and use tax is also specifically imposed over the purchase price for the use, storage or consumption of taxable transactions (as defined by the municipal internal regulation) taken place within Municipal limits. The Municipal Legislature approved the imposition of the municipal sales and use tax, effective on November 15, 2006.

On July 29, 2007 the Commonwealth Legislature approved Act No. 80 (“Act 80”) which amends Act No. 117 of July 4, 2006 to impose to all the Municipalities of Puerto Rico a uniform municipal sales and use tax of 1.5%. Effective August 1, 2007 1% of the 1.5% is collected by the Municipalities and the remaining .5% of the 1.5% is collected by the Puerto Rico Department of Treasury (PRDT). Act 80 also provides for restrictions on the use of the sales tax, which is required be invested in solid waste and recycling programs, capital improvements and health and public safety costs.

The amount collected by the PRDT (the remaining .5% of the 1.5%) is deposited in accounts or special funds in the Governmental Development Bank of Puerto Rico (“GDB”), subject to restrictions imposed and distributed as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE M – SALES AND USE TAXES - Continued

- a. .2% of the .5% will be deposited in a “Municipal Development Fund” to finance costs as restricted by the Act,
- b. .2% of the .5% will be deposited in a “Municipal Redemption Fund” to finance loans to Municipalities subject to restrictions imposed by the Act and,
- c. .1% of the .5% will be deposited in a “Municipal Improvement Fund” to finance capital improvement projects; these funds will be distributed based on legislation from the Commonwealth’s Legislature

The Municipal Legislature approved the Municipal Ordinance No. 15 Series 2007-2008 to conform to dispositions of Act 80.

Individuals, organizations and entities subject to collect the municipal sales and use tax must file a tax return to the Municipality. Tax is due each 20th day of each month based on tax collected in the preceding month. A total \$170,383 sales and use tax receivable represents the tax collected on June by individuals, organizations and entities but reported and paid to the Municipality on or before July 20, net of uncollectible accounts; \$57,089 and \$69,241 represents amounts of “Municipal Development Fund” and “Municipal Redemption Fund”, respectively collected on June by individuals, organizations and entities but paid by the PRDT subsequent to June 30. The amount of \$24,374 related to Municipal Development Fund and \$16,408 related to Municipal Redemption Fund are recorded as deferred revenue since are not available as required by current standards.

NOTE N – INTERGOVERNMENTAL REVENUES

Intergovernmental revenues in the General Fund are comprised of the following:

	<u>Amount</u>
Amount of municipal subsidies and equalization fund sent by CRIM	\$ 4,613,004
Compensation in lieu of tax from the Puerto Rico Electric Power Authority (PREPA)	1,937,440
Reimbursement from Commonwealth Government of Law 52 and Law 82 program expenditures	259,120
Reimbursement from Commonwealth Government of Christmas Bonus expenditures	287,453
Reimbursement from Commonwealth government – other programs expenditures	115,471
	<u>\$ 7,212,488</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE O – RETIREMENT PLAN

1. *Plan description*

Regular employees of the Municipality contribute to a cost-sharing multiple employer defined benefit retirement plan, administered by the Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS). ERS covers all regular full time public employees working for the central government, the municipalities and certain public corporations not having their own retirement systems. The system provides retirement pensions, death and disability benefits.

Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members of occupational and non occupational disabilities. Benefits vest after ten years of plan participation. The system was created under Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS.

Law No. 305 of September 24, 1999 amended the Act No. 447 of 1951 and was enacted with the purpose of establishing a new pension program (System 2000). The new pension program became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999 may elect either to stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000 will only be allowed to become members of the new program.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. There will be a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age will not be guaranteed by the State government and will be subjected to the total accumulated balance of the savings account. 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 employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. If the savings accounts balance is \$10,000 or less at time of retirement, the balance will be distributed by the System to the participant as a lump sum. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not been granted under the new program. The employer contributions (9.275% of the employee's salary) will be used to fund the current plan. Under System 2000 the retirement age is reduced from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE O – RETIREMENT PLAN - Continued

2. Funding policy

The Act 447, as amended, is the authority under which obligations to contribute to the Plan by the Plan members, employers and other contributing entities are established or may be amended. Plan members are required to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600 except for the Mayor or employee under a supplementation plan, which contributes 8.275% of gross salary. The Municipality is required to contribute 9.275% of gross salary.

The Municipality's actual contribution for the current and the previous three fiscal years, which is equal to the required contribution, follows:

<u>Fiscal year ended:</u>	<u>Law No. 447</u>	<u>System 2000</u>
2009	\$ 245,219	\$ 210,758
2008	\$ 241,665	\$ 148,108
2007	\$ 225,455	\$ 108,140

NOTE P – POSTEMPLOYMENT BENEFITS

In addition to the pension benefits described in Note O, the Municipality is required to cover annually the 3% increase in the retirement plan of its retired employees, as required by Commonwealth's laws. Also, the Municipality is required to finance costs related to the application of certain "Special Laws" issued by the Commonwealth Government. Those Special Laws granted increases in pensions and other benefits to retired employees of the Municipality such as medicines bonus, Christmas bonus and death benefits. For the fiscal year ended, costs related to these post employment benefits amounted to \$107,964.

NOTE Q – COMMITMENTS

1. Operating leases

The Municipality leases office space and office equipment under operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same terms. Rental expenses amounted approximately \$360,244. Management believes that the summary of the future minimum rental commitments under noncancelable equipment leases with terms exceeding one year is not significant.

2. Construction

The Municipality has commitments at June 30, 2009 of approximately \$5,576,370 for construction, improvements or renovation of certain capital assets.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE R – CONTINGENCIES

1. *Federal and Commonwealth grants*

Projects financed by Federal and Commonwealth's Grants are subject to audits by grantors and other governmental agencies in order to determine its expenditures to comply with the conditions of such grants. It is the Municipality's opinion that no additional material unrecorded liabilities will arise from audits previously performed or to perform.

2. *Litigations*

The Municipality is, at present, a defendant in a number of legal matters that arise in the ordinary course of the Municipality's activities. There are cases whereby the Municipality is a defendant or codefendant that will be covered by insurance and certain cases whereby the legal counsel has not determined an outcome. Of those not to be covered by insurance, the legal counsel has determined that it would be reasonably possible that in one case there may be an unfavorable outcome with an estimated loss ranging from \$30,000 to \$70,000. In addition, an estimated loss of \$3,000 is accrued in the government wide statements arising from a final settlement of one case to be paid subsequently by the Municipality. However, it is the opinion of the Municipality and the legal counsels that based on their experience, such actions and the potential liabilities will not impair the Municipality financial position.

NOTE S – PROPERTY LIEN

The Municipality entered into a financing agreement with the US Department of Housing and Urban Development (HUD) through a contract for Loan Guarantee Assistance under Section 108 of the Housing and Community Act of 1974, as amended. The agreement, for a maximum commitment of \$4,850,000 will finance the construction of a Youth Sports and Education Center. The repayment of funds is guaranteed through appropriation of funds from the Community Development Block Grant Program (Entitlement). As part of the contract agreement between HUD and the Municipality, additional guarantees are required. The Municipality should agree to declare and furnish to HUD, a property lien, satisfactory to HUD in form and substance of HUD's ownership interest in the property to be constructed (including land), specifying an estimate of fair market value of not less than \$6,062,500.

On June 29, 2009 the Municipality signed a deed of a voluntary first mortgage in the amount of \$6,062,500 in favor of HUD of all of its estate, right, title and interest in and to the Mortgaged Property, which includes the parcel of land on which the project is located and the property to be constructed. During the 20-year Section 108 note repayment term, it will not be permitted or suffered the use of any of the property for any purpose other than the use for which the same was intended at the time the Mortgage be executed. Upon default under the Contract for Loan Guarantee Assistance under Section 108, HUD, at its options, may declare the whole indebtedness secured to be due and payable, in which event HUD shall have the right immediately to foreclose the Mortgage.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO FINANCIAL STATEMENTS

June 30, 2009

NOTE T – FUND BALANCE DEFICITS

The Community Development Block Grant Program fund and certain special funds included as other governmental funds in the fund statements disclosed fund balance deficits as follows:

	Amount
Major Fund:	
CDBG	\$ 216,671
Other Governmental Funds:	
P.R. Traffic Safety Commission	\$ 20,540
Child Care (SENDEC and Summer Camp Funds)	\$ 225,852
DTOP	\$ 272,597
Office of Public Safety Affairs	\$ 32,200
P.R. Department of Family - Pres	\$ 83,133

The deficits result from the accrual of expenditures without accruing intergovernmental revenues for reimbursement of expenditures. As required by current standards, the Municipality recorded intergovernmental revenues for these reimbursement (expenditure-driven) grants on fund statements when all applicable eligibility requirements have been met and the resources are available.

NOTE U – FUND BALANCE AND NET ASSETS RESTATEMENT

The following table disclosed the change in fund balance and net assets balance at beginning of year as previously reported in the financial statements. The change resulted from the correction of an error in application of GASB 33 requirements to CDBG Fund and to recognize the net book value of a capital asset (machinery and equipment) not recorded in previous years. The beginning balance has been restated as follows:

Description	CDBG Fund Balance	Net assets, government wide statements
Balance at beginning of year, as previously reported	\$ (280,780)	\$ 53,057,975
Correction of errors, GASB 33	53,015	(1,852,935)
Book value, capital asset	-	324,502
Balance at end of year, as restated	\$ (227,765)	\$ 51,529,542

REQUIRED SUPPLEMENTARY INFORMATION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2009

	Budgeted amounts		Actual Amounts (Budgetary Basis) (See Note A)	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Taxes:				
Property taxes	\$ 4,796,236	\$ 5,080,226	\$ 5,080,226	\$ -
Municipal license taxes	2,226,561	2,561,696	2,567,760	6,064
Sales and use taxes	2,060,000	2,206,332	2,493,733	287,401
Intergovernmental	5,166,510	5,165,668	5,451,212	285,544
Fees, fines and charges for services	723,658	1,853,949	1,843,216	(10,733)
Interest	100,000	100,000	351,536	251,536
Other	50,000	145,719	291,137	145,418
Total revenues	<u>15,122,965</u>	<u>17,113,590</u>	<u>18,078,820</u>	<u>965,230</u>
Expenditures:				
Current:				
General government	8,384,580	8,246,165	7,776,608	469,557
Public works and sanitation	2,653,886	2,756,234	2,670,659	85,575
Public safety	970,642	995,050	965,119	29,931
Culture and recreation	592,969	596,456	560,059	36,397
Health	628,315	628,315	608,428	19,887
Housing, welfare and community development	1,367,573	1,375,745	1,254,363	121,382
Total expenditures	<u>14,597,965</u>	<u>14,597,965</u>	<u>13,835,236</u>	<u>762,729</u>
Excess of revenues over expenditures	525,000	2,515,625	4,243,584	1,727,959
Other financing sources (uses):				
Transfers out	(525,000)	(2,515,625)	(2,515,625)	-
Total other financing sources (uses)	<u>(525,000)</u>	<u>(2,515,625)</u>	<u>(2,515,625)</u>	<u>-</u>
Excess of revenues and other financing sources over expenditures and other financing uses	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,727,959</u>	<u>\$ 1,727,959</u>

The accompanying notes to required supplemental information are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -
BUDGETARY COMPARISON SCHEDULE – GENERAL FUND**

June 30, 2009

NOTE A – BUDGET PROCESS AND BUDGETARY BASIS OF ACCOUNTING

The Municipal budget is prepared for the General Fund following the requirements of the Autonomous Municipal Law of 1981, as amended. It is developed utilizing elements of performance-based program budgeting and zero-based budgeting and includes estimates of revenues and other sources for ensuing fiscal year under laws existing at the time the budget is prepared.

Budget amendments are approved by the Municipal Legislature. Certain budget transfers within the limitations and restrictions of the Municipal Law can be approved by the Mayor or by the Municipal Legislature. The budget comparison schedule provides information about the original budget, the amended budget and the actual results, under the budgetary basis of accounting.

The budgetary basis of accounting is different from GAAP. Revenues are generally recorded when cash is received and expenditures are generally recorded when the related expenditure is incurred or encumbered. The encumbrances (that is, purchase orders, contracts) are considered expenditures when a commitment is made. On a GAAP basis, encumbrances outstanding at year end are reported in the governmental funds statements as a reservation of fund balance since they do not constitute expenditures or liabilities while on a budgetary basis encumbrances are recorded as expenditures of current year. Encumbrance appropriations lapse one year after the end of the fiscal year. Unencumbered appropriations are lapsed at year-end. The legal level of budgetary control (the level at which expenditures may not legally exceed appropriations) is at the function level.

The presentation of the budgetary data excludes other appropriations such as capital projects, debt service and special revenue funds because projects are funded on a multi-year nature, generally requiring several years to complete or effective budgetary control is alternatively achieved through general obligation bond indentures and legal and contractual grant agreement provisions.

NOTE B - BUDGET TO GAAP RECONCILIATION

The accompanying budgetary comparison schedule presents comparisons of the original and final legally adopted budget with actual data on a budgetary basis. Since accounting principles applied for the purposes of developing data on a budgetary basis differ significantly from those used to present accounting principles generally accepted in the United States, the following budget to GAAP reconciliation is presented:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION -
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND**

June 30, 2009

NOTE B - BUDGET TO GAAP RECONCILIATION - Continued

Excess of revenues and other financing sources over expenditures and other financing uses (budgetary basis):	\$ 1,727,959
Budget to GAAP differences:	
Entity differences:	
Non-budgeted funds recorded as revenues for financial reporting purposes:	2,616,014
Non-budgeted funds recorded as expenditures for financial reporting:	(4,298,613)
Non budgeted proceeds from issuance of general obligation bonds:	-
Non-budgeted transfers in:	1,897,447
Non-budgeted transfers out:	(63,568)
Basis of accounting differences:	
Revenues recorded for financial reporting purposes but not in budgetary basis:	450,094
Expenditures recorded in budgetary basis but not for financial reporting purposes:	503,395
Expenditures recorded for financial reporting purposes but not in budgetary basis:	(143,561)
Revenues recorded in budgetary basis but not for financial reporting purposes:	(528,277)
Timing differences:	
Current year encumbrances recorded as expenditures for budgetary reporting purposes:	182,444
Prior year encumbrances recorded as expenditures for financial reporting purposes:	(118,236)
Net change in fund balance (GAAP basis):	<u>\$ 2,225,098</u>

SUPPLEMENTARY INFORMATION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2009

Line Item No.	Description	14,871
		Housing Choice Vouchers
Balance Sheet		
111	Cash - unrestricted	\$ 186,968
113	Cash - other restricted	\$ 69,596
100	Total cash	\$ 256,564
121	Accounts receivable - PHA projects	\$ 1,284
122	Accounts receivable - HUD other projects	\$ 176
125	Accounts receivable - miscellaneous	\$ 484
126.2	Allowance for doubtful accounts - other	\$ (1,768)
120	Total receivables, net of allowance for doubtful accounts	\$ 176
150	Total Current Assets	\$ 256,740
164	Furniture, equipment and machinery - administration	\$ 26,002
166	Accumulated depreciation	\$ (9,405)
160	Total capital assets, net of accumulated depreciation	\$ 16,597
180	Total Non-current Assets	\$ 16,597
190	Total Assets	\$ 273,337
312	Accounts payable <= 90 days	\$ 2,579
322	Accrued compensated absences - current portion	\$ 2,964
345	Other current liabilities	\$ 8,932
347	Inter-program - due to	\$ 98,180
310	Total Current Liabilities	\$ 112,655
300	Total Liabilities	\$ 112,655
508.1	Invested in Capital Assets, Net of Related Debt	\$ 16,597
511.1	Restricted Net Assets	\$ 67,586
512.1	Unrestricted Net Assets	\$ 76,499
513	Total Equity/Net Assets	\$ 160,682
600	Total Liabilities and Equity/Net Assets	\$ 273,337
Income Statement		
70600-010	Housing assistance payments	\$ 267,588
70600-020	Ongoing administrative fees earned	\$ 52,839
70600-070	Admin fee calculation description	
70600	HUD PHA operating grants	\$ 320,427
71500	Other revenue	\$ 10,131
700	Total Revenue	\$ 330,558
91100	Administrative salaries	\$ 31,315
91200	Auditing fees	\$ 5,000
91500	Employee benefit contributions- administrative	\$ 3,882
91600	Office expenses	\$ 3,008
91800	Travel	\$ 3,167
91000	Total Operating - Administrative	\$ 46,372
96200	Other general expenses	\$ 504
96210	Compensated absences	\$ 1,548
96600	Bad debt - other	\$ 1,768
96000	Total Other General Expenses	\$ 3,820
96900	Total Operating Expenses	\$ 50,192
97000	Excess Revenue Over Operating Expenses	\$ 280,366

The accompanying notes are an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE
BALANCE SHEET AND STATEMENT OF REVENUES AND EXPENSES INFORMATION
JUNE 30, 2009

Line Item No.	Description	14.871 Housing Choice Vouchers
Balance Sheet		
97300-050	All Other	\$ 293,394
97300	Housing assistance payments	\$ 293,394
97350	HAP Portability-in	\$ 8,912
97400	Depreciation expense	\$ 1,906
97500	Fraud losses	\$ -
900	Total Expenses	\$ 354,404
10000	Excess (Deficiency) of Revenue Over (Under) Expenses	\$ (23,846)
11030	Beginning equity	\$ 184,528
11040-010	Prior period adjustments and correction of errors - Editable	\$ -
11040	Prior period adjustments, equity transfers, and correction of errors	\$ -
11770-001	Administrative Fee Equity - Beginning Balance	\$ 91,136
11170-010	Administrative Fee Revenue	\$ 52,839
11170-020	Hard to House Fee Revenue	\$ -
11170-021	FSS Coordinator Grant	\$ -
11170-030	Audit Costs	\$ -
11170-040	Investment Income	\$ -
11170-045	Fraud Recovery Revenue	\$ -
11170-050	Other Revenue	\$ 10,131
11170-051	Comment For Other Revenue	This amount corresponds to the administrative fees earned on the portability-in vouchers administered by the Municipality (\$1,219) plus the reimbursement received from the initial PHAs of the HAP rent payments made on behalf of the portability-in units during 08-09 (\$8,912)
11170-060	Total Admin Fee Revenues	\$ 62,970
11170-080	Total Operating Expenses	\$ 50,192
11170-090	Depreciation	\$ 1,906
11170-095	Housing Assistance Portability In	\$ 8,912
11170-100	Other Expenses	\$ -
11170-101	Comment For Other Expense	
11170-110	Total Expenses	\$ 61,010
11170-002	Net Administrative Fee	\$ 1,960
11170-003	Administrative Fee Equity - Ending Balance	\$ 93,096
11170	Administrative Fee Equity	\$ 93,096
11180-001	Housing Assistance Payments Equity - Beginning Balance	\$ 93,392
11180-010	Housing Assistance Payments Revenues	\$ 267,588
11180-015	Fraud Recovery Revenue	\$ -
11180-020	Other Revenue	\$ -
11180-021	Comment For Other Revenue	
11180-025	Investment Income	\$ -
11180-030	Total HAP Revenues	\$ 267,588
11180-080	Housing Assistance Payments	\$ 293,394
11180-090	Other Expenses	\$ -
11180-091	Comment For Other Expense	
11180-100	Total Housing Assistance Payments Expenses	\$ 293,394
11180-002	Net Housing Assistance Payments	\$ (25,806)
11180-003	Housing Assistance Payments Equity - Ending Balance	\$ 67,586
11180	Housing Assistance Payments Equity	\$ 67,586
11190-210	Total ACC HCV Units	1,032
11190-220	Unfunded Units	-
11190-230	Other Adjustments	-
11190	Unit Months Available	1,032
11210	Unit Months Leased	946

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTE TO SUPPLEMENTARY INFORMATION - FINANCIAL DATA SCHEDULE

June 30, 2009

NOTE A – BASIS OF PRESENTATION

The accompanying financial data schedule (FDS) is a trial balance of the Section 8 Housing Choice Voucher Program administered by the Municipality. The FDS was created in order to standardize the financial information reported by Public Housing Authorities (PHA) to the Real Estate Assessment Center (REAC), as required by the Uniform Financial Reporting Standards (UFRS). REAC is the US Department of Housing and Urban Development (HUD) national management center created to assess the condition of HUD owned and assisted properties. The UFRS are rules to implement requirements of 24 CFR, Part 5, Subpart H, for the electronic filing of financial information to HUD.

In accordance with the guidelines for reporting and attestation requirements of UFRS, the accompanying FDS is included as information supplementary to the financial statements. It was prepared using the accrual basis of accounting, as required by REAC regulations.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

COMBINED BALANCE SHEET-
SPECIAL FUNDS IN GENERAL FUND
JUNE 30, 2009

<u>Assets</u>	<u>General Fund (01)</u>	<u>Special Funds Unreserved-GF</u>	<u>Special Funds Designated-GF</u>	<u>Special Funds Reserved</u>	<u>Subtotal</u>	<u>Eliminations</u>		<u>Total General Fund</u>
Cash and investments	\$ 10,083,632	\$ 3,524,462	\$ 4,236,322	\$ -	\$ 17,844,416	\$ -	\$ -	\$ 17,844,416
Receivables, net:								
Municipal License Taxes	4,774	-	-	-	4,774	-	-	4,774
Sales and use taxes	227,472	-	-	-	227,472	-	-	227,472
Other	155,509	99,705	-	-	255,214	-	-	255,214
Due from:								
Commonwealth Government	764,920	149,077	27,760	-	941,757	-	-	941,757
Other funds	3,986,157	-	400,000	-	4,386,157	-	2,492,336	1,893,821
Inventories and Supplies	-	203,557	-	-	203,557	-	-	203,557
Restricted assets:								
Cash	-	-	-	157,106	157,106	-	-	157,106
Total assets	\$ 15,222,464	\$ 3,976,801	\$ 4,664,082	\$ 157,106	\$ 24,020,453	\$ -	\$ 2,492,336	\$ 21,528,117
 Liabilities and Fund Balances								
Liabilities:								
Accounts payable and accrued liabilities	\$ 471,885	\$ 93,683	\$ 205,476	\$ 12,975	784,019	\$ -	\$ 1	\$ 784,020
Due to:								
Commonwealth Government	127,039	-	-	-	127,039	-	-	127,039
Federal Government	-	-	119,160	-	119,160	-	-	119,160
Other funds	-	1,869,642	622,695	9,068	2,501,405	2,492,337	-	9,068
Advances from other funds	1,307,498	-	-	-	1,307,498	-	-	1,307,498
Deferred revenues:								
Municipal license taxes	2,010,302	-	-	-	2,010,302	-	-	2,010,302
Sales and use tax	24,374	-	-	-	24,374	-	-	24,374
Commonwealth Government	716,079	56,903	27,760	-	800,742	-	-	800,742
Other	140,064	33,216	-	-	173,280	-	-	173,280
Total liabilities	4,797,241	2,053,444	975,091	22,043	7,847,819	2,492,337	1	5,355,483
 Fund balance:								
Reserved for:								
Inventories	-	203,557	-	-	203,557	-	-	203,557
Encumbrances	182,444	-	-	-	182,444	-	-	182,444
Other specific purposes	-	-	-	135,063	135,063	-	-	135,063
Unreserved:								
Designated for future years expenditures	-	-	3,688,991	-	3,688,991	-	-	3,688,991
Undesignated	10,242,779	1,719,800	-	-	11,962,579	-	-	11,962,579
Total fund balances	10,425,223	1,923,357	3,688,991	135,063	16,172,634	-	-	16,172,634
Total liabilities and fund balances	\$ 15,222,464	\$ 3,976,801	\$ 4,664,082	\$ 157,106	\$ 24,020,453	\$ 2,492,337	\$ 2,492,337	\$ 21,528,117

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES-
SPECIAL FUNDS IN GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2009

	General Fund (01)	Special Funds Unreserved-GF	Special Funds Designated-GF	Special Funds Reserved	Subtotal	Eliminations		Total General Fund
Revenues:								
Taxes:								
Property taxes	\$ 3,577,940	\$ -	\$ -	\$ -	\$ 3,577,940	\$ -	\$ -	\$ 3,577,940
Municipal license taxes	2,567,760	-	-	-	2,567,760	-	-	2,567,760
Sales and use taxes	2,479,233	-	-	-	2,479,233	-	-	2,479,233
Intergovernmental:								
Commonwealth government	6,837,897	268,267	-	106,324	7,212,488	-	-	7,212,488
Fees, fines and charges for services	1,892,057	2,200,351	-	-	4,092,408	-	-	4,092,408
Interest	149,760	26,892	-	-	176,652	-	-	176,652
Other	352,481	-	14,180	-	366,661	-	-	366,661
Total revenues	17,857,128	2,495,510	14,180	106,324	20,473,142	-	-	20,473,142
Expenditures:								
Current:								
General government	7,943,257	318,157	876,521	-	9,137,935	-	-	9,137,935
Public works and sanitation	2,637,125	63,062	390,807	-	3,090,994	-	-	3,090,994
Public safety	967,128	-	-	-	967,128	-	-	967,128
Culture and recreation	557,394	-	-	-	557,394	-	-	557,394
Health	608,428	2,154,842	-	12,975	2,776,245	-	-	2,776,245
Housing, welfare and community development	1,254,363	-	59,340	43,184	1,356,887	-	-	1,356,887
Capital outlays	2,620	225,488	143,657	10,580	382,345	-	-	382,345
Total expenditures	13,970,315	2,761,549	1,470,325	66,739	18,268,928	-	-	18,268,928
Excess (deficiency) of revenues over expenditures	3,886,813	(266,039)	(1,456,145)	39,585	2,204,214	-	-	2,204,214
Other financing sources (uses):								
Payment of P.R.E.P.A. debt	(105,879)	-	-	-	(105,879)	-	-	(105,879)
Transfers in	143,509	410,423	1,487,024	-	2,040,956	1,914,193	-	126,763
Transfers out	(1,850,625)	(16,746)	(46,822)	-	(1,914,193)	-	(1,914,193)	-
Total other financing sources (uses)	(1,812,995)	393,677	1,440,202	-	20,884	1,914,193	(1,914,193)	20,884
Net change in fund balances	2,073,818	127,638	(15,943)	39,585	2,225,098	1,914,193	(1,914,193)	2,225,098
Fund balances at beginning of year	8,351,405	1,795,719	3,704,934	95,478	13,947,536	-	-	13,947,536
Fund balances at end of year	\$ 10,425,223	\$ 1,923,357	\$ 3,688,991	\$ 135,063	\$ 16,172,634	\$ 1,914,193	\$ (1,914,193)	\$ 16,172,634

SINGLE AUDIT SECTION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FISCAL YEAR ENDED JUNE 30, 2009

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number (note B)	Pass-Through Entity Identifying Number (note C)	Federal Expenditures (note A)
<u>U.S. Department of Agriculture</u>			
Passed through the P.R. Department of Education: Child and Adult Care Food Program	10.558	CCC-205	\$ 77,511
<u>U.S. Department of Housing and Urban Development</u>			
Community Development Block Grant - Entitlement Grants	14.218	N/A	1,518,071
Passed through the Office of Commissioner of Municipal Affairs: Community Development Block Grant - State's Program	14.228	FD-32, AB-32 FC-32, AF-32	464,367
Passed through the P.R. Department of Housing: Home Investment Partnership Program	14.239	N/A/V	87,851
Community Development Block Grant_ Section 108 Loan Guarantees	14.248	N/A	230,416
Section 8 Housing Choice Vouchers	14.871	N/A	320,427
Subtotal U.S. Department of Housing and Urban Development			<u>2,621,132</u>
<u>U.S. Department of Transportation - National Highway Traffic Safety Administration</u>			
Passed through the P.R. Department of Transportation - (Traffic Safety Commission) State and Community Highway Safety	20.600	N/A/V	51,388
<u>U.S. Department of Health and Human Services</u>			
Passed through the P.R. Department of Family - Families and Children Administration: Child Care and Development Block Grant	93.575	N/A/V	301,596
Head Start Program	93.600	N/A	747,602
Subtotal U.S. Department of Health and Human Services			<u>1,049,198</u>
<u>U.S. Department of Homeland Security</u>			
Passed through the Puerto Rico Governor Office - (Office of Public Safety Affairs):			
Citizen Corps	97.053	2004-GE-T4-0008	121,323
State Homeland Security Program (SHSP)	97.073	2007-GE-T7-0043	20,850
Law Enforcement Terrorism Prevention Program (LETPP)	97.074	2007-GE-T7-0043	11,360
Subtotal U.S. Department of Homeland Security			<u>153,533</u>
Total Expenditures of Federal Awards			<u>\$ 3,952,762</u>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2009

NOTE A – BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality and is presented on the modified accrual basis of accounting. Expenditures are recognized when the related liability is incurred. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, "Audits of States, Local Governments and Nonprofit Organizations". Therefore, some amounts presented in this schedule may differ from the amounts presented in, or used in the preparation of, the basic financial statements.

NOTE B - FEDERAL CFDA NUMBER

The Catalog of Federal Domestic Assistance (CFDA) Number is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence.

NOTE C – PASS-THROUGH ENTITY IDENTIFYING NUMBER

State or local government redistributions of federal awards to the Municipality, known as "pass-through awards", should be treated by the Municipality as though they were received directly from the federal government. OMB Circular A-133 requires the schedule to include the name of the pass-through entity and the identifying number assigned by the pass-through entity for the federal awards received as a subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

NOTE D – RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS

Description	Community Development Block Grant Fund	Head Start Program Fund	Other Governmental Funds
10.558	\$ -	\$ -	\$ 77,511
14.218	1,518,071	-	-
14.228	464,367	-	-
14.239	-	-	87,851
14.248	-	-	230,416
14.871	-	-	320,427
20.600	-	-	51,388
93.575	-	-	301,596
93.600	-	747,602	-
97.053	-	-	121,323
97.073	-	-	20,850
97.074	-	-	11,360
Total federal awards expenditures	1,982,438	747,602	1,222,722
Adjustment for Section 8 HCV	-	-	31,016
Total nonfederal awards expenditures	-	-	1,692,638
Total expenditures, fund statements	<u>\$ 1,982,438</u>	<u>\$ 747,602</u>	<u>\$ 2,946,376</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2009

NOTE E – OTHER: LOAN GUARANTEE LOAN OUTSTANDING

The Municipality received on October 1, 2007 \$1,200,000 on advance funds under a \$1,345,000 variable/fixed rate note dated July 12, 2007 to finance the construction of a Youth Sports and Education Center. The Municipality expended \$230,416 from these proceeds during fiscal year 2008-2009. The following represents the loan outstanding balance as of June 30, 2009:

<u>CFDA No.</u>	<u>Program Name</u>	<u>Loan outstanding balance</u>
14.248	Community Development Block Grants_ Section 108 Loan Guarantees	<u>\$ 1,200,000</u>

VALDES, GARCIA, MARIN & MARTINEZ, LLP

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

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

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Isabela (the Municipality) as of and for the year ended June 30, 2009, which collectively comprise the Municipality's basic financial statements, and have issued our report thereon dated December 23, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

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

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

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

Compliance and other matters

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

We noted certain matters that we reported to the management of the Municipality in a separate letter dated December 23, 2009.

This report is intended solely for the information and use of the Municipality's management, the Honorable Mayor and Members of the Municipal Legislature, the Commonwealth of Puerto Rico 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.

Valdes, Garcia, Marin + Martinez, LLP

San Juan, Puerto Rico
December 23, 2009

Stamp 2474905 was
affixed to the original.

VALDES, GARCIA, MARIN & MARTINEZ, LLP

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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

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

Compliance

We have audited the compliance of Municipality of Isabela (the Municipality) 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, 2009. The Municipality'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 grant agreements and other matters applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on the Municipality's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Municipality's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Municipality's compliance with those requirements.

In our opinion, the Municipality of Isabela complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2009-1 and 2009-2.

Internal Control Over Compliance

The management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grant agreements and other matters applicable to federal programs. In planning and performing our audit, we considered the Municipality's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over compliance.

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

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material non-compliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

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

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

This report is intended solely for the information and use of the Municipality's management, the Honorable Mayor and Members of the Municipal Legislature, the Commonwealth of Puerto Rico 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.

Valdes, Garcia, Marin & Martinez, LLP

San Juan, Puerto Rico
December 23, 2009

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to the original.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I - Summary of Auditors' Results

FISCAL YEAR ENDED JUNE 30, 2009

I. Summary of auditors' results:

Part I - Financial Statements

1. Type of auditors' report issued: Unqualified opinion Qualified opinion
 Adverse opinion Disclaimer of opinion

Internal control over financial reporting:

2. Significant deficiencies identified? Yes No
3. Significant deficiencies reported as material weaknesses? Yes None reported
4. Financial statements material noncompliance noted? Yes No

Part II - Federal Awards

Internal control over major programs:

1. Significant deficiencies identified? Yes No
2. Significant deficiencies reported as material weaknesses? Yes None reported
3. Type of auditors' report issued on compliance of major programs: Unqualified opinion Qualified opinion
 Adverse opinion Disclaimer of opinion
4. Any audit findings required to be reported under Section 510(a) of OMB Circular A-133? Yes No

5. Identification of major programs (Section 520 (h) (i) of OMB Circular A-133):

CFDA Number(s)	Name of Federal Program or Cluster
14.218	Community Development Block Grants - Entitlement Grants
14.871	Section 8 Housing Choice Vouchers
93.600	Head Start Program
93.575	Child Care and Development Grant

6. Dollar threshold used to distinguish between Type A and Type B programs: \$300,000
7. Auditee qualified as Low-risk auditee? Yes No

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section II - Financial Statements Findings

FISCAL YEAR ENDED JUNE 30, 2009

Finding	No matters reported.
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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section III Federal Awards Findings and Questioned Costs

FISCAL YEAR ENDED JUNE 30, 2009

Reference Number: 2009-1

Agency: U.S. Department of Housing and Urban Development

Award: Community Development Block Grant/Entitlement Grants

CFDA Number: 14.218

Compliance Requirement: Procurement

Condition

We found that the Municipality did not include in the construction contracts a provision for compliance with the Copeland "Anti-Kickback" Act and the Contract Work Hour and Safety Standards Act sections 103 and 107 for the Llanadas Park Recreational Facilities Improvements and the Rehabilitation of Houses, Capiro Sector Project .

Criteria

2 CFR Part 215 Appendix A to Part 215 Contract Provisions establishes in paragraphs number two and four the following:

All contracts awarded by a recipient including small purchases, shall contain the following provisions as applicable:

Copeland "Anti-Kickback" Act – All contracts and sub grants in excess of \$2,000 for construction or repair awarded by recipients and sub-recipients shall include a provision for compliance with the Copeland "Anti-kickback" Act. The Act provides that each contractor or sub-recipient shall be prohibited from inducing, by any means, any person employed in the construction completion, or repair of public work, to give up any part of the compensation to which he is otherwise entitled.

Contract Work Hours and Safety Standards Act – All contracts awarded by recipients in excess of \$2,000 for construction contracts and in excess of \$2,500 for other contracts that involve the employment of mechanics or laborers shall include a provision for compliance with sections 103 and 107 of the Contract Work Hour and Safety Standards Act. Under section 103 of the Act, each contractor shall be required to compute the wages of every mechanic and laborer on the basis of a standard work week of 40 hours. Section 107 of the Act is applicable to construction work and provides that no laborer or mechanic shall be required to work in surroundings or under working conditions which are unsanitary, hazardous or dangerous.

Effect

The Municipality failed to direct the contractor to avoid that any person give up any part of the compensation for the contracted work , that wages of every mechanic or laborer be computed on the basis of a standard work week of 40 hours and that laborers or mechanics should not work under conditions which are unsanitary, hazardous or dangerous.

(Continues)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section III Federal Awards Findings and Questioned Costs

FISCAL YEAR ENDED JUNE 30, 2009

Reference Number: 2009-1 (Continued)

Cause

The management of the Municipality is using the state regulation of the Controller Office for contract provisions. As a consequence, the previously indicated federal regulations are not included in the construction contracts examined during the audit.

Questioned Costs

None

Recommendation

The Municipality should include the Copeland "Anti-kickback" Act provisions and Sections 103 and 107 of the Contract Work Hour and Safety Standards Act to comply with federal regulations.

Response

The Municipal Secretary and Federal Program Director have been instructed that all contracts must comply with federal regulations. However, as part of the corrective action, the Municipal Secretary revised the compliance of other active federal contracts and all comply with the federal regulations (Copeland "Anti-kickback" Act provisions and Sections 103 and 107 of the Contract Work Hours and Safety Standards Act). So, the contracts mentioned in the finding are an isolated mistake that will be amended if they are not defeated.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section III Federal Awards Findings and Questioned Costs

FISCAL YEAR ENDED JUNE 30, 2009

Reference Number: 2009-2

Agency: U.S. Department of Health and Human Services

Award: Child Care and Development Block Grant

CFDA Number: 93.575

Compliance Requirement: Reporting

Condition

We found that the Municipality submitted the quarterly reports for Fund request (Form CC-004) of October 2008, January 2009 and April 2009 to ACUDEN (Sub-grantor) with a delay of 62, 74 and 119 days, respectively. The report of July 2009 had not been prepared at the time of our audit tests.

Criteria

The contract between the Municipality and ACUDEN states in clause number 7, that Fund requests will be submitted in advance by the Municipality to ACUDEN during the first ten calendar days of October, January, April and July of the contract year.

Effect

The Municipality is not in compliance with the requirements established by the Sub-grantor.

Cause

The Municipality did not establish good internal control procedures to avoid delays in the submission of the reports to the Sub-grantor.

Questioned Costs

None

Recommendation

The Municipality should establish internal control procedures to comply with the requirements of the Subgrantor regarding the timely submission of the Fund request reports.

Response

The Finance Director has been instructed to submit reports within the first ten days after the quarter end. The report of July 2009 was submitted to the agency (ACUDEN).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF ISABELA**

**SCHEDULE OF STATUS OF PRIOR YEAR AUDIT FINDINGS AND QUESTIONED COSTS
FISCAL YEAR ENDED JUNE 30, 2009**

Finding Number	Program	Noncompliance	Corrective Action Plan	Questioned Costs	Status
08-1	Section 8 Housing Choice Voucher Program (CFDA No. 14.871)	Special Test and Provisions – Utility Allowance Schedule	Program’s management has been instructed to follow the program requirements regarding this and any other compliance. The Finance and Section 8 Program Directors are under direct supervision to the Municipality program’s officers in charge of the study for the final completion and submission of the Utility Data Schedule to US HUD. In addition, annual updates have been programmed in the months of November of each year if there is a change above of 10% cost benchmark. This monitoring process will be performed by Municipality program’s officers.	None	Program’s Management submitted a new Utility Allowance Schedule, effective on October 1, 2008 and this action was accepted by HUD in letter dated October 28, 2008.