

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

MUNICIPIO DE LAJAS
AUDITORIA 2002-2003
30 DE JUNIO DE 2003

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LAJAS**

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

FISCAL YEAR ENDED JUNE 30, 2003

TABLE OF CONTENTS

	<u>PAGE</u>
I. FINANCIAL SECTION:	
Independent Auditors' Report	1
General Purpose Financial Statements	
Combined Balance Sheet - All Governmental Fund Types and Account Groups	3
Combined Statement of Revenues, Expenditures and Changes in Fund Balances - All Governmental Fund Types	5
Combined Statement of Revenues and Expenditures - Budget and Actual - General and Debt Service Funds	6
Notes to Financial Statements	7
Supplemental Information	
Schedule of Expenditures of Federal Awards	25
Notes to Schedule of Expenditures of Federal Awards	26
II. REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS	28
III. REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133	30
IV. SCHEDULE OF FINDINGS AND QUESTIONED COSTS	32
V. SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS	34

INDEPENDENT AUDITORS' REPORT

Mayor and Municipal Legislature
Municipality of Lajas
Lajas, Puerto Rico

We have audited the accompanying general purpose financial statements of the Municipality of Lajas, Puerto Rico, as of and for the year ended June 30, 2003, as listed in the table of contents. These general purpose financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these general purpose financial statements based on our audit.

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 general purpose financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall general purpose financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the Municipality of Lajas, Puerto Rico, as of June 30, 2003, and the results of its operations 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 October 3, 2003 on our consideration of the Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Our audit was performed for the purpose of forming an opinion on the general purpose financial statements of the Municipality of Lajas, Puerto Rico, taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget and Circular A-133 "Audits of States, Local Governments, and Non-Profit Organizations", and is not a required part of the general purpose financial statements. Such information in that schedule has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly stated in all material respects, in relation to the general purpose financial statements taken as a whole.



Rodriguez, Rivera & Toro LLP

MUNICIPALITY OF LAJAS

COMBINED BALANCE SHEET - ALL GOVERNMENTAL FUND TYPES AND ACCOUNT GROUPS

June 30, 2003

	Governmental Funds				Account groups		Total (Memorandum only)
	General	Special Revenue	Debt Service	Capital Project	General Fixed Assets	General Long- Term Debt	
ASSETS AND OTHER DEBITS							
Cash and short term investments	\$ 46,333	\$ 434,680	\$ -	\$ 2,582,839	\$ -	\$ -	\$ 3,063,852
Cash with fiscal agent	-	368,477	931,167	587,310	-	-	1,886,954
Receivables (net where applicable of allowance for uncollectibles)							
Property tax	-	-	44,825	-	-	-	44,825
Municipal License tax	730	-	-	-	-	-	730
Due from:							
Commonwealth governmental entities	634,379	149,045	-	-	-	-	783,424
Federal grants	-	33,246	-	-	-	-	33,246
Other funds	213,849	-	-	-	-	-	213,849
Property, plant and equipment	-	-	-	-	21,472,950	-	21,472,950
Amount available in debt service fund	-	-	-	-	-	649,490	649,490
Amount to be provided for retirement of general and special obligation bonds and notes	-	-	-	-	-	2,339,510	2,339,510
Amount to be provided for retirement of other long-term debt	-	-	-	-	-	4,258,974	4,258,974
Total assets and other debits	\$ 895,291	\$ 985,448	\$ 975,991	\$ 3,170,149	\$21,472,950	\$ 7,247,974	\$ 34,747,805

The accompanying notes are an integral part of these general purpose financial statements.

MUNICIPALITY OF LAJAS

COMBINED BALANCE SHEET - ALL GOVERNMENTAL FUND TYPES AND ACCOUNT GROUPS

June 30, 2003

	Governmental Funds				Account groups		Total (Memorandum only)
	General	Special Revenue	Debt Service	Capital Project	General Fixed Assets	General Long- Term Debt	
LIABILITIES							
Accounts payable	\$ 408,244	\$ 45,496	\$ -	\$ 20,777	\$ -	\$ -	\$ 474,518
Accrued payroll taxes and withholdings	32,592	-	-	-	-	-	32,592
Matured bonds and notes payable	-	-	235,000	-	-	-	235,000
Matured interest payable	-	-	46,676	-	-	-	46,676
Due to:							
Commonwealth governmental entities	47,449	-	-	-	-	-	47,449
Other funds	-	213,849	-	-	-	-	213,849
Deposits payable	49,411	-	-	-	-	-	49,411
Deferred revenues:							
Municipal license taxes	393,323	-	-	-	-	-	393,323
Intergovernmental - Commonwealth entities	160,935	-	-	-	-	-	160,935
Federal grants	-	374,453	-	-	-	-	374,453
General and special obligations bonds and notes	-	-	-	-	-	2,989,000	2,989,000
Other long-term debt	-	-	-	-	-	4,258,974	4,258,974
Total liabilities	1,091,954	633,798	281,676	20,777	-	7,247,974	9,276,180
FUND EQUITY AND OTHER CREDITS							
Investment in general fixed assets	-	-	-	-	21,472,950	-	21,472,950
Fund balance							
Reserved for:							
Encumbrances	36,674	-	-	-	-	-	36,674
Debt service	-	-	694,315	-	-	-	694,315
Capital projects	-	-	-	3,149,372	-	-	3,149,372
Other purposes	-	351,651	-	-	-	-	351,651
Unreserved							
Undesignated	(233,337)	-	-	-	-	-	(233,337)
Total fund equity and other credits	(196,663)	351,651	694,315	3,149,372	21,472,950	-	25,471,625
Total liabilities, fund equity and other credits	\$ 895,291	\$ 985,448	\$ 975,991	\$ 3,170,149	\$ 21,472,950	\$ 7,247,974	\$ 34,747,805

The accompanying notes are an integral part of these general purpose financial statements.

MUNICIPALITY OF LAJAS

COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - ALL GOVERNMENTAL FUND TYPES

FISCAL YEAR ENDED JUNE 30, 2003

	Governmental Funds				Total (Memorandum only)
	General	Special Revenue	Debt Service	Capital Projects	
Revenues					
Property taxes	\$ 1,970,186	\$ -	\$ 335,205	\$ -	\$ 2,305,391
Municipal license taxes, licenses and permits	1,007,183	-	-	-	1,007,183
Intergovernmental	3,943,279	3,030,643	-	2,650,265	9,624,187
Rental income of properties	478,014	-	-	-	478,014
Fines and forfeitures	1,514	-	-	-	1,514
Interest	16,492	7,262	9,646	44,609	78,008
Other	525,237	-	-	-	525,237
Total revenues	7,941,904	3,037,904	344,852	2,694,873	14,019,534
Expenditures					
Current:					
General government	2,927,654	1,833,698	-	-	4,761,352
Public safety	137,160	255,139	-	-	392,298
Sanitation and public works	3,502,336	6,205	-	-	3,508,541
Health	339,233	-	-	-	339,233
Welfare	383,128	916,109	-	-	1,299,237
Culture and recreation	490,171	771	-	-	490,942
Education	223,687	14,302	-	-	237,989
Other	-	-	37,181	-	37,181
Capital outlays	-	783,594	-	1,451,057	2,234,651
Debt service					
Principal	-	-	339,000	-	339,000
Interest	-	-	160,925	-	160,925
Total expenditures	8,003,368	3,809,819	537,106	1,451,057	13,801,350
Excess (deficiency) of revenues over expenditures	(61,463)	(771,915)	(192,254)	1,243,816	218,184
Other financing sources (uses)					
Bond anticipation notes	-	-	-	274,313	274,313
Operating transfers in	61,940	-	-	-	61,940
Operating transfers out	-	7,262	10,069	44,609	61,940
Total other financing sources (uses)	61,940	(7,262)	(10,069)	229,704	274,313
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	476	(779,177)	(202,323)	1,473,520	492,497
Fund balance at beginning of year, as restated	(197,139)	1,130,827	896,638	1,675,851	3,506,177
Fund balance at end of year	\$ (196,663)	\$ 351,651	\$ 694,315	\$ 3,149,372	\$ 3,998,674

The accompanying notes are an integral part of these general purpose financial statements.

MUNICIPALITY OF LAJAS

COMBINED STATEMENT OF REVENUES AND EXPENDITURES - BUDGET AND
ACTUAL - GENERAL AND DEBT SERVICE FUNDS

FISCAL YEAR JUNE 30, 2003

	General Fund		Variance Favorable (Unfavorable)	Debt Service		Variance Favorable (Unfavorable)
	Budget	Actual		Budget	Actual	
Revenues						
Property taxes	\$ 1,972,382	\$ 1,970,186	\$ (2,196)	\$ 312,421	\$ 335,205	\$ 22,784
Municipal license taxes, licenses and permits	930,239	1,087,017	156,778	-	-	-
Intergovernmental	3,907,926	3,943,279	35,353	-	-	-
Rental income of properties	346,816	427,835	81,019	-	-	-
Fines and forfeitures	500	1,514	1,014	-	-	-
Interest	52,839	78,431	25,592	-	9,646	9,646
Other	573,444	575,415	1,971	-	-	-
	<u>7,784,146</u>	<u>8,083,678</u>	<u>299,532</u>	<u>312,421</u>	<u>344,852</u>	<u>32,431</u>
Expenditures						
General government	2,998,482	2,964,328	34,155	-	37,181	(37,181)
Public safety	146,953	137,160	9,793	-	-	-
Sanitation and public works	3,479,307	3,502,336	(23,028)	-	-	-
Health	345,939	339,233	6,706	-	-	-
Welfare	392,654	383,128	9,526	-	-	-
Culture and recreation	495,320	490,171	5,150	-	-	-
Education	225,491	223,687	1,804	-	-	-
Debt service						
Principal	-	-	-	154,722	339,000	(184,278)
Interest	-	-	-	157,699	160,925	(3,226)
Transfers to other funds	-	-	-	-	10,069	(10,069)
Total expenditures	<u>8,084,146</u>	<u>8,040,042</u>	<u>44,104</u>	<u>312,421</u>	<u>547,175</u>	<u>(234,754)</u>
Excess (deficiency) of revenues over expenditures	(300,000)	43,636	343,636	-	(202,323)	(202,323)
Fund balance allocation	<u>300,000</u>	<u>-</u>	<u>(300,000)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	<u>\$ -</u>	<u>\$ 43,636</u>	<u>\$ 43,636</u>	<u>\$ -</u>	<u>\$ (202,323)</u>	<u>\$ (202,323)</u>

The accompanying notes are an integral part of these general purpose financial statements.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Lajas was founded in 1883. 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 twelve (12) 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. A summary of the Municipality's significant accounting policies consistently applied in the preparation of the accompanying general purpose financial statements follows:

1. *Financial reporting entity*

The financial reporting entity included in this report consists of the financial statements of the Municipality of Lajas (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. 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 exist between the primary government and the potential component unit.

There are two methods of presentation of the component unit in the financial statement:

- a. Blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances.
- b. Discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions:

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

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

2. *Basis of presentation*

The financial transactions of the Municipality are recorded in individual funds and account groups. 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. The various funds and account groups are reported by generic classification within the financial statements. Amounts in the "Total (Memorandum Only)" columns in the general purpose financial statements represent a summation of the financial statement line items of the fund types and account groups and are presented for information purposes only. This total includes fund types and account groups that use different basis of accounting and interfund transactions that have not been eliminated and the caption "amounts to be provided", which is not an asset in the usual sense. Consequently, amounts shown in the "Total (Memorandum Only)" columns are not comparable to a consolidation and do not represent the total resources available or total revenues and expenditures of the Municipality. The following fund types and account groups are used by:

a. **Governmental Funds**

Governmental Funds are those through which most governmental functions of the Municipality are financed. The acquisition, uses, and balances of the Municipality expendable financial resources and the related liabilities are accounted for through governmental funds. The measurement focus is upon determination of changes in financial position rather than upon net income determination. The following are the Municipality's Governmental Fund Types:

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

Special Revenue Funds. Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than major capital projects) that are legally restricted to expenditures for specified purposes.

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

Capital Projects Funds. Capital Projects Funds is used to account for financial resources to be used for the acquisition or construction of major capital facilities.

b. **Account Groups**

Accounts Groups are used to establish accounting control and accountability for the Municipality's general fixed assets and general long-term debts. The following are the Municipality's accounts groups:

General Fixed Assets Accounts Group. This group of accounts is established to maintain control and cost information account for all fixed assets of the Municipality. General Fixed Assets are recorded as expenditures of the various Municipality funds at the time of purchase and are subsequently capitalized for memorandum purposes in the General Fixed Assets Accounts Group.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Such assets include land, buildings, building improvements, furniture and equipment, roads, streets, sidewalks, bridges and lighting systems. No depreciation is provided on General Fixed Assets. General fixed assets are capitalized at historical cost or estimated historical cost if historical cost is not available. Donated fixed assets are valued at their estimated fair market value on donation date.

General Long-Term Debt Accounts Group. This group of accounts is established to account for all long-term debts of the Municipality. Because of their spending measurement focus, expenditures recognition for governmental fund types is limited to exclude amounts represented by non current liabilities. Since they do not affect net current assets, such long-term amounts are not recognized as governmental fund type expenditures or fund liabilities. They are instead reported as liabilities in the General Long-Term Debt Accounts Group.

3. Measurement focus and basis of accounting

a. Governmental Funds

Governmental funds are accounted for using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are included on the balance sheet in the general purpose financial statements. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets. The governmental funds statements are maintained and reported on the modified accrual basis of accounting. Under this method of accounting, revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Municipality considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when the related liability is incurred.

Property taxes are recognized as revenues in the year for which they are levied. Revenues on intergovernmental grants are recognized when all eligibility requirements (which include time requirements) imposed by the provider have been met and revenue becomes available. For certain expenditure-driven grants revenue is recognized after allowable expenditures are incurred. Licenses and permits, charges for services, rent and miscellaneous revenues are recorded as revenues when received because they are not measurable and available.

The Municipality reports deferred revenues in the governmental funds statements which arise when potential revenue does not meet both measurable and available criteria for recognition in the current period. 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.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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) 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.

4. *Budget process and budgetary basis of accounting*

The Municipal budget is prepared for General Fund and the Debt Service Fund following the requirements of the Municipal Law of 1981 as amended. Although all operating expenses and expenditures are allocated to departmental operating budgets, certain items are not considered to be subject to direct control at the department level. These includes: terminal leave payments, payroll taxes, pension costs, court costs and settlements, telephone and electricity expenses and liability, workers compensation and property insurance premiums. Budget amendments, which require a change in total appropriations of any department, are approved by the Municipal Legislature. Amendments to current year budget with prior year's budgetary surpluses, if any, are recorded in the Combined Statement of Revenues and Expenditures Budget and Actual - General and Debt Service Fund as "Fund Balance Allocation". Certain budget transfers within the limitations and restriction of the Municipal Law can be approved by the Executive Branch or by the Legislature Branch. The budget is prepared on a budgetary (statutory) basis of accounting which is different from GAAP. Revenues include amounts classified by GAAP as other financing sources and expenditures include encumbrances and amounts classified by GAAP as other financing uses. 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 presentation of the budgetary data excludes other appropriations such as capital projects 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.

5. *Cash, cash equivalents and cash with fiscal agent*

Cash and cash equivalents consists of cash on hand, demand deposits and short term investments with original maturities of three months or less from the date of acquisition. The Municipality follows the practice of pooling cash of all funds except for certain state grants, restricted funds generally held by outside custodians and federal grants. Available pooled cash balance beyond immediate needs is invested in certificates of deposits.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Cash with fiscal agent in the debt service fund consists of the undisbursed balance of property 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. Cash with fiscal agent in the special revenue and capital project funds represents the undisbursed proceeds from general and special obligation bonds and notes and certain grants which are maintained in a cash custodian account by the Governmental Development Bank of Puerto Rico (GDB).

6. *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 Commonwealth Governmental Entities in the general fund represents contributions from the Puerto Rico Electric Power Authority (PREPA) for payments in lieu of tax and/or represents amounts due from the Municipal Revenues Collection Center (CRIM) for excess of actual collections over advances of property taxes and amounts of municipal equalization fund ; in the special revenue fund represents amounts owed to the Municipality for reimbursement of expenditures incurred on Commonwealth agencies grants. 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 tax revenue of current fiscal year collected by the CRIM on the first month (July) of subsequent fiscal year.

7. *Interfund receivables and payables*

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due 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 between funds are reported as "due from/to other funds".

8. *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.

9. *Compensated absences*

The Municipality's employee accumulates vacation and sick leave based on continuous service. The vacation and sick leave for employees are accumulated on the basis of 2½ days per month of vacation and 1½ days per month of sick pay 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 pay is liquidated to employees with 10 years or more service up to the maximum number of days. The amount of vacations leave is accrued if earned based on services already performed by employees and if it is probable that will be paid in a future period. The amount of sick leave is accrued based on all vesting amounts for which payment is probable and on accumulated benefits as of the fiscal year-end.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

The accrual of compensated absences includes estimated payments that are related to payroll. The current portion of unpaid compensated absences is recorded as a fund liability if the amount is expected to be paid using expendable available financial resources. The non-current portion is reported on the General Long-Term Debt Account Group since it is anticipated that none of the liability will be liquidated with expendable financial resources. Vacations and sick leave, when paid, are recorded as expenditures in the General Fund.

10. Fund balance

a. Reservation of fund balance

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

- 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.
- Debt Service: Represents 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 purposes Represents net assets legally segregated for other specific future uses

11. Interfund transactions

The Municipality reports certain transactions as operating transfers, which are legally required transfers that are reported when incurred as "Operating transfers-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.

12. Risk financing

The Puerto Rico Treasury Department (PRDT) acts as an agent, obtaining and determining the coverage for the municipalities of Puerto Rico. The coverage for the Municipality of Lajas consists of professional, public responsibility, property and theft, auto and fidelity bond coverage.

Insurance policies costs are allocated by PRDT among all the municipalities of Puerto Rico. Payment of the Municipality's insurance premiums is monthly deducted from advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM). Workers compensation insurance is also deducted from the monthly advances by the CRIM. Settled cases have not exceeded insurance coverage for any of the past three years.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

13. *Use of estimates*

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

14. *Future adoption of accounting pronouncements*

In June 1999, the GASB issued Statement No. 34, "*Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*" which affects the way the Municipality prepares and presents financial information. This Statement, which establishes new requirements and a new reporting model for the annual reports of state and local governments, was developed to make annual reports easier to understand and more useful to the people who use the governmental financial information to make decisions. The Municipality is required to implement GASB 34 on fiscal year ended June 30, 2004.

Other GASB Statements are required to be implemented in conjunction with GASB 34. Therefore, the Municipality will implement the following GASB Statements in the fiscal year ended June 30, 2004: GASB Statement No. 37 "*Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus—an amendment of GASB Statements No. 21 and No. 34*"; GASB Statement No. 38 "*Certain Financial Statement Note Disclosures*"; and GASB Statement No. 41 "*Budgetary Comparison Schedules—Perspective Differences—an amendment of GASB Statement No. 34*".

The GASB has issued other statements, which the Municipality has not yet adopted:

	Statement	To be Adopted in Fiscal year ended,
39	Determining Whether Certain Organizations Are Component Units - an amendment of GASB 34 Statement No. 14	June 30, 2004
40	Deposit and Investment Risk Disclosure - an amendment of GASB Statement No. 3	June 30, 2005

The impact of these statements on the Municipality's basic financial statement has not yet been determined.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE B - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

1. *Budget to GAAP reconciliation*

The Municipality's Combined Statement of Revenues, Expenditures and Changes in Fund Balances - All Governmental Fund Types has been prepared in accordance with GAAP and the Combined Statement of Revenues and Expenditures Budget and Actual - General and Debt Service Fund has been prepared on the 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:

Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses (Budgetary basis)	\$ 43,636
Add: Expenditures recognized under Budgetary-statutory basis but not accrued under GAAP basis by the Municipality	36,674
Revenues recognized under GAAP basis but not under budgetary basis	730
Less: Revenues recognized under Budgetary basis but not under GAAP basis	<u>(80,564)</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses (GAAP basis)	<u>\$ 476</u>

2. *Excess of expenditures over appropriations*

The sanitation and public works expenditures category in the general fund disclosed excess of expenditures over appropriations in the Statement of Revenues and Expenditures budget and actual. The excess occurred primarily due to charges for expenditures related to utilities (electricity).

3. *Fund balance allocation*

The Statement of Revenues and Expenditures budget and actual present a fund balance allocation of \$300,000. This represents a readjustment of current year budget with prior year's budgetary surpluses, approved by Resolution Number 5 of September 12, 2002 and Resolution Number 15 of December 1, 2002 of the Municipal Legislature.

NOTE C - DEPOSITS AND SHORT TERM INVESTMENTS

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 are held by the Secretary of Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Governmental Development Bank of Puerto Rico (GDB).

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE C - DEPOSITS AND SHORT TERM INVESTMENTS - Continued

The Municipality's bank balances in commercial banks of \$3,759,639 were fully collateralized at June 30, 2003. The deposits at GDB of \$954,536 reported in the special revenue and capital project funds and \$931,167 that are reported in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

The cash and short term investments balance of the general fund includes \$45,600 invested in the Puerto Rico Government Investment Trust Fund (PRGITF). The PRGITF was created by the Secretary of the Treasury of the Commonwealth pursuant to Act No. 176, of August 11, 1995, and began operations on December 4, 1995. PRGITF is a no-load diversified collective investment trust administered by the Government Development Bank of Puerto Rico that was created for the purpose of providing eligible governmental investors of Puerto Rico to invest in a money market portfolio. The deposits on hand and the investments purchased are not collateralized, secured or guaranteed by the Commonwealth or any of its agencies, instrumentalities or political subdivisions.

The PRGITF invests in short-term instruments, which may be considered highly liquid as defined by the limitations contained in Rule 2a-7 of the Investment Company Act of 1940. However, the investments are subject to the ability of the PRGITF to receive payment from the securities' issuer when due. The Municipality investment is recorded at cost in the general purpose financial statements, which is not significantly different from investment pool's share price. Income earned from the investments made by the PRGITF is available for withdrawal at any time.

NOTE D - RECEIVABLES

1. *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, 2003 the tax rates were as follows:

Financial business - 1.50% of gross revenues

Other organizations - .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 \$393,323 are recorded as deferred revenues.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE D - RECEIVABLES - Continued

2. *Due from Commonwealth entities*

Amounts due from Commonwealth entities as of June 30, 2003 follows:

Description	General Fund	Special Revenue Fund
Municipal Revenue Collection Center (CRIM) - excess of actual property tax collections over advances of property tax and amounts of municipal equalization fund	\$ 160,935	\$ -
Puerto Rico Electric Power Authority (PREPA) - settled legal case (see note O)	473,444	-
Puerto Rico Department of Labor - payroll and related liabilities under Law No. 52	-	149,045
Total:	<u>\$ 634,379</u>	<u>\$ 149,045</u>

The amount due from CRIM is recorded as deferred revenue since is not available as required by current standards.

NOTE E - INTERFUND TRANSACTIONS

1. *Due from/to other funds:*

Amounts due from/to other funds represent temporary advances to other funds by the general fund payroll and payroll taxes expenditures, as follows:

Receivable Fund	Payable Fund	Amount
General Fund	Special revenue fund-Law No. 52	\$ 125,049
General Fund	Special revenue fund-Child Care	45,516
General Fund	Special revenue fund-Various	43,284
Total:		<u>\$ 213,849</u>

2. *Operating transfers:*

Transfers between individual funds were made for operational purposes. Transfers include interest earned on cash with fiscal agents in the special revenue, debt service and capital project funds which is transferred to the general fund.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE F - PROPERTY, PLANT AND EQUIPMENT

A summary of the General Fixed Assets Accounts Group transactions follows:

	Balance July 1, 2002	Increases	Decreases	Other adjustments	Balance June 30, 2003
Land	\$ 1,293,910	\$ -	\$ -	\$ (342,158)	\$ 951,752
Land improvements	-	-	-	61,016	61,016
Construction in progress	-	224,402	-	-	224,402
Buildings and building improvements	13,959,920	-	-	(6,980,320)	6,979,600
Infrastructure	1,798,199	-	-	7,896,987	9,695,186
Vehicles, machinery and equipment	2,868,318	1,099,233	-	(406,557)	3,560,994
Total	<u>\$ 19,920,347</u>	<u>\$ 1,323,635</u>	<u>\$ -</u>	<u>\$ 228,968</u>	<u>\$ 21,472,950</u>

The Municipality performed a physical inventory of fixed assets and a review of general fixed asset records. As a result of this process, adjustments were necessary which are identified as "other adjustments".

NOTE G - DEFERRED REVENUES

Deferred revenues for Commonwealth agencies represent resources received before the Municipality has a legal claim to them and for federal grants represent resources that are received before allowable expenditures are incurred. A detail of these balances follows:

Fund/Grant	General Fund	Special Revenue Fund
Due from CRIM	\$ 160,935	\$ -
Federal Emergency Management Agency (FEMA)	-	278,425
Child Care and Development Block Grant	-	93,661
Community Development Block Grant (CDBG)	-	1,826
Other	-	541
Total:	<u>\$ 160,935</u>	<u>\$ 374,453</u>

NOTE H - LONG TERM DEBT

1. Changes in general long term debt

The following summarizes activity in the general long term debt account group for the fiscal year ended June 30, 2003:

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE H - LONG TERM DEBT - Continued

	Balance at July 1, 2002	Increases	Decreases	Balance at June 30, 2003
General, Special Obligations Bonds and Notes	\$ 3,548,000	\$ -	\$ 559,000	\$ 2,989,000
Other long term debt	1,432,285	2,852,321	25,632	4,258,974
	<u>\$ 4,980,285</u>	<u>\$ 2,852,321</u>	<u>\$ 584,632</u>	<u>\$ 7,247,974</u>

2. *General and special obligation bonds and notes*

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2003 amount to \$2,989,000. 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 levy and collect property taxes for payment of principal and interest on bonds and notes. A debt service fund has been established for the bonds and notes at GDB with the proceeds of those property taxes, whereby sufficient funds must be set aside in order to cover the projected debt service requirement, before any new bonds are issued. The Municipality is required to maintain a legal debt margin of 10% of the total assessment of property located within the Municipality plus the balance of the property taxes in the debt service fund.

A detail of the general and special obligation bonds and notes as of June 30, 2003 follows:

	Outstanding Amount
1996 general obligation bonds of \$415,000 due in annual installments of \$10,000 to \$40,000 through July 1, 2013; bearing interest at rates ranging from 4.7% to 6.58%	\$ 305,000
1994 public improvement bonds of \$435,000 due in annual installments of \$15,000 to \$50,000 through July 1, 2008; bearing interest at rates ranging from 6.106% to 7.606%	210,000
1996 general obligation bonds of \$1,000,000 due in annual installments of \$24,000 to \$66,000 through January 1, 2021; with interest at 4.5%	839,000
2000 general obligation notes of \$478,000 due in annual installments of \$59,000 to \$78,000 through January 1, 2007; with interest at 5%	292,000
2000 general obligation notes of \$70,000 due in annual installments of \$9,000 to \$12,000 through January 1, 2007; with interest at 5%	43,000
2000 general obligation notes of \$880,000 due in annual installments of \$150,000 to \$205,000 through July 1, 2006; bearing interest at rates ranging from 2.7% to 5%	570,000

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE H - LONG TERM DEBT – Continued

	Outstanding Amount
2001 general obligation bonds of \$770,000 due in annual installments of \$20,000 to \$75,000 through July 1, 2020; bearing interest at rates ranging from 2.7% to 5.29%	730,000
	\$ 2,989,000

The annual requirement to amortize general and special obligation bonds and notes as of June 30, 2003 follows:

June 30	Principal	Interest
2004	\$ 359,000	\$ 139,371
2005	394,000	124,934
2006	415,000	108,782
2007	221,000	91,106
2008	147,000	79,211
Thereafter	1,453,000	489,939
Totals	\$ 2,989,000	\$ 1,033,343

3. *Other long-term liabilities*

	Amount
Compensated absences - includes accrued vacations, sick leave benefits and other benefits with similar characteristics, represents the Municipality's commitment to fund such costs from future operations.	\$ 1,448,513
Estimated closure and post-closure care costs of Municipal Landfill - State and Federal laws and regulations require the Municipality to place a final cover on its landfill when closed and perform certain maintenance and monitoring 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 futures closure and post-closure care costs that will be incurred near or after the date the landfill no longer accepts waste. The Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to comply with applicable laws and regulations. As 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	

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE H - LONG TERM DEBT - Continued

	<u>Amount</u>
landfill closure and post-closure care costs has a balance of \$1,277,703 as of June 30, 2003, which is based on 73% usage of the landfill. It is estimated that an additional \$476,005 will be recognized as closure and post-closure care expenditures between the date of the balance sheet and the date the landfill is expected to be filled to capacity (December 2012). The estimated total current costs of the landfill closure and post-closure care (\$1,753,708) 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, 2003. 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, 2003 the Municipality has not made contributions to finance closure and post-closure care costs.	1,277,703
Claims and judgments - represent the final settlement of two legal cases paid subsequent to June 30, 2003 for a total amount of \$64,000 plus an amount of \$78,054 payable to a construction contractor. The amount payable to the contractor was subsequently refinanced through the issuance by GDB of a \$625,000 loan. (see note N)	142,054
Bond anticipation notes (BAN) - the Municipality intends refinancing of the BAN's on a long-term basis. It has demonstrated its intention and its ability to consummate by a financing agreement with the Governmental Development Bank of Puerto Rico (GDB) to issue a \$563,000 general obligation bond, which does not expire within one year from the date of the combined balance sheet.	274,313
Compensatory time - amount payable to Municipal employees since previous years. Amount was subsequently refinanced through the issuance by GDB of a \$625,000 loan. (see note O).	483,048
Payable to CRIM - prior year's doubtful accounts - As of June 30, 2002 the Municipality has entered into an agreement with the Municipal Revenue Collection Center (CRIM) to refinance the prior year's property tax doubtful accounts, which amounted to \$312,069 on a long-term basis. It has demonstrated its intentions and its ability to consummate the transaction by an agreement with the CRIM which does not expire within one year from the date of the combined balance sheet under the provision of Law No. 146 of October 11, 2001. The refinancing will be done through a special loan to be repaid from .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico's general fund. The financing agreement was authorized by the Municipal Legislature of Lajas on Resolution No. 62 of March 13, 2002.	312,069

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE H - LONG TERM DEBT - Continued

	<u>Amount</u>
Advances from CRIM (Law No. 42) - represents the balance owed to CRIM at June 30, 2003 for excess of advances of property tax and other subsidies over final amount of property tax collections for the fiscal year ended June 30, 2000 (see note I). This amount will be repaid with operational 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) - (see note I)	<u>321,274</u>
	<u>\$ 4,258,974</u>

NOTE I - PROPERTY TAXES

The Municipal Revenue Collection Center (CRIM) (a state governmental agency) is responsible for the assessment, collection and distribution of real and personal property taxes in accordance with the Municipal Property Tax Law (Law 83 of August, 1995). The tax levied on property is determined by the Municipal Government based on limits established by the Commonwealth Legislature. 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. Real property is assessed by the CRIM. The tax is general assessed on January 1 on all taxable property located within the Municipality. 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.

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. The Municipality has a net payable to the CRIM of \$321,274 pertaining to previous fiscal years. A receivable of \$160,935 resulting from the final settlement for fiscal year 2002-2003 is recorded as deferred revenue since is not available as required by current standards.

NOTE J - INTERGOVERNMENTAL REVENUES

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

	<u>Amount</u>
Amount of municipal subsidies sent by CRIM	\$ 2,963,468
Compensation in lieu of tax from the Puerto Rico Electric Power Authority (PREPA)	888,601
Reimbursement from Commonwealth Government of Christmas Bonus expense	<u>91,210</u>
	<u>\$ 3,943,279</u>

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE K - FUND BALANCE RESTATEMENTS

Beginning fund balances of governmental funds has been restated to reflect the correction of errors and recognition of certain assets and liabilities not recorded in previous year. Detail of restatements follows:

	General Fund	Special Revenue Fund	Debt Service Fund	Capital Project Fund
Fund balance at beginning of year, as previously reported:	\$ 1,269,328	\$ -	\$ 1,171,079	\$ 1,535,632
Adjustments:	<u>(1,466,467)</u>	<u>1,130,827</u>	<u>(274,441)</u>	<u>140,219</u>
Fund balance at end of year, as restated	<u>\$ (197,139)</u>	<u>\$ 1,130,827</u>	<u>\$ 896,638</u>	<u>\$ 1,675,851</u>

NOTE L - 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 as its Instrumentalities (ERS). ERS covers all regular full time public employees working for the central government, public corporations and the municipalities of Puerto Rico. 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 no 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 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

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE L - RETIREMENT PLAN - Continued

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.

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 two fiscal years, which is equal to the required contribution, follows:

<u>Fiscal year ended:</u>	<u>Law No. 447</u>	<u>System 2000</u>
2003	\$ 224,322	\$ 10,629
2002	\$ 229,149	N/A
2001	\$ 237,263	N/A

NOTE M - COMMITMENTS

1. Operating leases

The Municipality leases 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 to \$3,424. Management believes that the summary of the future minimum rental commitments under noncancelable equipment leases with terms exceeding one year is not significant.

NOTE N - CONTINGENCIES

1. Federal and State grants

Projects financed by Federal and State 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.

Municipality of Lajas

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE N - CONTINGENCIES - Continued

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, certain cases whereby the legal counsel has not determined an outcome and other cases that will not be covered by insurance. As a result of two settled cases subsequent to June 30, 2003 and not to be covered by insurance, the Municipality accrued \$64,000 in the general long term debt account group. 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 O - SUBSEQUENT EVENTS

1. On July 15, 2003 the Municipality received \$473,444 from the Puerto Rico Electric Power Authority (PREPA) related to a settled legal case against PREPA by the Municipality's of Puerto Rico.
2. On October 6, 2003, the Government Development Bank of Puerto Rico approved a \$625,000 loan to the Municipality for the payment of compensatory time, the completion of an infrastructure project, and the payment of judgment and claims. Loan will be repaid with from general fund 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).

SUPPLEMENTAL INFORMATION

MUNICIPALITY OF LAJAS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FISCAL YEAR ENDED JUNE 30, 2003

Federal Grantor/Pass-Through Grantor Program Title	Federal CFDA Number (Note B)	Pass-Through Grantor's Number (Note C)	Expenditures (Note A)
<u>U.S. Department of H.U.D.</u>			
Major Program:			
Passed through the Office of Commissioner of Municipal Affairs:			
Community Development Block Grant - State's Program	14.228	AB-36 FD-36 FC-36	\$ 968,955
Nonmajor Program:			
Direct Program:			
Section 8 Housing Choice Vouchers	14.871	N/A	283,032
			<u>1,251,987</u>
<u>U.S. Department of Agriculture</u>			
Nonmajor Programs:			
Direct Program:			
Water and Waste Disposal System for Rural Communities	10.760	N/A	295,090
Passed through the P.R. Department of Family:			
Child and Adult Care Food Program	10.558	N/AV	9,460
			<u>304,550</u>
<u>Federal Emergency Management Agency</u>			
Passed through the Puerto Rico Governor Office: (Governor's Authorized Representative-GAR)			
Public Assistance Grants	83.544	DR-PR-1247	113,897
Public Safety Partnership and Community Policing Grants-COPS	16.710	98UMWX2379	176,575
<u>U.S. Department of Health and Human Services</u>			
Nonmajor Program:			
Passed through the P.R. Department of Family - Families and Children Administration:			
Child Care and Development Block Grant	93.575	N/AV	365,672
<u>U.S. Department of Transportation</u>			
Nonmajor program:			
Direct Program:			
Federal Transit Capital Improvement Grants	20.500	N/A	208,957
<u>U.S. Department of Labor</u>			
Nonmajor program:			
Passed through the Southwestern Consortium:			
WIA Youth Activities	17.259	N/AV	41,701
Total federal awards expenditures			<u>\$ 2,463,339</u>

The accompanying notes are an integral part of this schedule.

Municipality of Lajas

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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 Government and Nonprofit Organizations.

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 GRANTOR'S 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 federal awards received as a subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

Municipality of Lajas

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2003

NOTE D - RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE GENERAL PURPOSE FINANCIAL STATEMENTS

<u>Description</u>	<u>Special Revenue Fund</u>
14.228	\$ 968,955
14.871	283,032
10.760	295,090
10.558	9,460
83.544	113,897
16.710	176,575
93.575	365,672
20.500	208,957
17.259	<u>41,701</u>
Total federal awards expenditures:	2,463,339
Total state funds awards expenditures and other nonfederal expenditures:	<u>1,346,480</u>
Total expenditures, general purpose financial statements	<u>\$ 3,809,819</u>

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

Mayor and Municipal Legislature
Municipality of Lajas
Lajas, Puerto Rico

We have audited the general purpose financial statements of the Municipality of Lajas, as of and for the year ended June 30, 2003, and have issued our report thereon dated October 3, 2003. 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.

Compliance

As part of obtaining reasonable assurance about whether Municipality of Lajas' general purpose financial statements are free of material misstatement, we performed test of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests did not disclose instances of noncompliance that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of non compliance that we have reported to the management of the Municipality of Lajas in a separate letter dated October 3, 2003.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Municipality of Lajas' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the general purpose financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted certain matters involving internal control over financial reporting that we have reported to management of the Municipality of Lajas, in a separate letter dated October 3, 2003.

This report is intended for the information of the Municipal Legislature, Management, Federal and Commonwealth awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.



Rodriguez, Rivera & Toro LLP

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

Mayor and Municipal Legislature
Municipality of Lajas
Lajas, Puerto Rico

Compliance

We have audited the compliance of Municipality of Lajas 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, 2003. Municipality of Lajas' major federal programs are identified in the Summary of Auditor's Results Section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Municipality of Lajas' management. Our responsibility is to express an opinion on Municipality of Lajas' compliance based on our audit.

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

In our opinion, the Municipality of Lajas 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, 2003.

Internal Control Over Compliance

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

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over compliance that we have reported to the management of Municipality of Lajas in a separate letter dated October 3, 2003.

This report is intended for the information of the Municipal Legislature, Management, Federal and Commonwealth awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.



Rodriguez, Ruelma E. Toro MP

Municipality of Lajas

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year ended June 30, 2003

I. Summary of audit results:

Part I - Financial Statements

1. Type of audit report: Unqualified opinion Qualified opinion
 Adverse opinion Disclaimer of opinion
2. Reportable conditions reported as a material weakness: Yes No
3. Material noncompliance disclosed: Yes No

Part II - Federal Awards

1. Reportable conditions reported as a material weakness: Yes No
2. Type of report on compliance for major programs: Unqualified opinion Qualified opinion
 Adverse opinion Disclaimer of opinion
3. Audit findings required to be reported under Section 510(a) of Circular A - 133: Yes No

4. Major programs:

CFDA Number(s)	Name of Federal Program or Cluster
14.228	Community Development Block Grant - State's Program
93.575	Child Care and Development Block Grant

5. Dollar threshold used to distinguish Type A and Type B programs: \$300,000 \$3,000,000
 \$30,000,000
6. Low-risk auditee: Yes No

Municipality of Lajas

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

II. Findings related to the financial statements reported in accordance with GAGAS:

None to be reported

III. Findings and questioned costs for federal awards:

None to be reported

Municipality of Lajas

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year ended June 30, 2003

There were no prior year findings to be followed-up as disclosed in the prior year audit report.

