

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

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

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CORREOS DE PUERTO RICO

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF LUQUILLO

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2002

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF LUQUILLO

YEAR ENDED JUNE 30, 2002

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF LUQUILLO

YEAR ENDED JUNE 30, 2002

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Luquillo
Luquillo, Puerto Rico**

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

Except as discussed in the following paragraph, we conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the provisions of the Office of Management and Budget 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 the general-purpose financial statements are free of material misstatement. 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 statements presentation. We believe that our audit provides a reasonable basis for our opinion.

The **Municipality of Luquillo** accounting system and subsidiary records of property and equipment did not provide us sufficient competent evidence with respect to the amounts presented in the accompanying general-purpose financial statements. Therefore, we do not express an opinion on such amounts included in the general fixed assets account group.

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

INDEPENDENT AUDITORS' REPORT (Continued)

In accordance with *Government Auditing Standards*, we have also issued our report dated November 22, 2002 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 grants.

Our audit was performed for the purpose of forming an opinion on the general-purpose financial statements of the **Municipality of Luquillo**, taken as whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the general purpose financial statements. The 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 presented, in all material respects, in relation to the general purpose financial statements taken as a whole.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
November 22, 2002

Stamp No. 1854010 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO
COMBINED BALANCE SHEET
ALL GOVERNMENTAL FUND TYPES AND ACCOUNT GROUPS
JUNE 30, 2002**

	GOVERNMENTAL FUND TYPES				ACCOUNT GROUPS		TOTALS (MEMORANDUM ONLY)
	General	Special Revenue	Debt Service	Capital Projects	General Fixed Assets	General Long-term Debt	
ASSETS AND OTHER DEBITS							
Cash	\$2,121,616	\$725,714		\$346,076			\$3,193,406
Cash with fiscal agent		398,528	\$1,734,737	391,101			2,524,366
Intergovernmental receivables	24,829	33,050					57,879
Federal grants receivable		163,876					163,876
Due from other funds	458,434			26,232			484,666
Property and equipment					\$13,342,970		13,342,970
Amount available in Debt Service Fund						\$1,734,737	1,734,737
Amount to be provided for retirement of general long-term debt						2,272,198	2,272,198
Total assets and other debits	\$2,604,879	\$1,321,168	\$1,734,737	\$763,409	\$13,342,970	\$4,006,935	\$23,774,098
LIABILITIES AND FUND EQUITY							
Liabilities:							
Accounts payable and accrued liabilities	\$285,195	\$63,501					\$348,696
Due to other funds	19,232	465,434					484,666
Due to other governmental entities	14,049					\$891,453	905,502
Deferred municipal license tax revenues	405,097						405,097
Deferred federal grant revenues		401,518					401,518
General obligation bonds						1,970,000	1,970,000
Notes Payable						480,000	480,000
Accrued compensated absences						637,982	637,982
Claims and Judgments						27,500	27,500
Total liabilities	723,573	930,453				4,006,935	5,660,961
Fund equity:							
Investment in general fixed assets					\$13,342,970		13,342,970
Fund balances:							
Reserved for encumbrances	876,933						876,933
Reserved for debt service			\$1,734,737				1,734,737
Unreserved:							
Designated for specific fund purposes		390,715		\$763,409			1,154,124
Undesignated	1,004,373						1,004,373
Total fund equity	1,881,306	390,715	1,734,737	763,409	13,342,970		18,113,137
Total liabilities and fund equity	\$2,604,879	\$1,321,168	\$1,734,737	\$763,409	\$13,342,970	\$4,006,935	\$23,774,098

See accompanying notes to general purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO
COMBINED STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
ALL GOVERNMENTAL FUND TYPES
YEAR ENDED JUNE 30, 2002**

	GOVERNMENTAL FUND TYPES				TOTALS (MEMORANDUM ONLY)
	General	Special Revenue	Debt Service	Capital Projects	
REVENUES					
Property taxes	\$2,601,347		\$984,785		\$3,586,132
Municipal license taxes	666,330				666,330
Licenses and permits	386,623				386,623
Intergovernmental	2,305,920	\$194,420		\$351,088	2,851,428
Rent of property	28,450				28,450
Fines and penalties	280				280
Interest	46,952				46,952
Federal grants		1,191,299			1,191,299
Miscellaneous	300,664	14,178			314,842
Total revenues	<u>6,336,566</u>	<u>1,399,897</u>	<u>984,785</u>	<u>351,088</u>	<u>9,072,336</u>
EXPENDITURES					
Current:					
Mayor and Municipal Assembly	636,345				636,345
General government	2,160,230	82,419			2,242,649
Public safety	119,460	4,540			124,000
Public works	1,600,733	46,486			1,647,219
Public health and sanitation	244,691				244,691
Welfare	636,735	751,562			1,388,297
Economic development	32,148	372,503			404,651
Recreation	254,992	10,399			265,391
Debt service:					
Principal retirement			329,000		329,000
Interest			156,236		156,236
Capital outlays	77,853	368,375		665,177	1,111,405
Total expenditures	<u>5,763,187</u>	<u>1,636,284</u>	<u>485,236</u>	<u>665,177</u>	<u>8,549,884</u>
Excess (deficiency) of revenues over (under) expenditures	<u>573,379</u>	<u>(236,387)</u>	<u>499,549</u>	<u>(314,089)</u>	<u>522,452</u>
OTHER FINANCES SOURCES (USES):					
Operating transfer to other funds	(37,320)				(37,320)
Operating transfer from other funds			37,320		37,320
Total other financing sources (uses)	<u>(37,320)</u>		<u>37,320</u>		<u>-</u>
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing sources (uses)	536,059	(236,387)	536,869	(314,089)	522,452
Fund balances, beginning as restated	<u>1,345,247</u>	<u>627,102</u>	<u>1,197,868</u>	<u>1,077,498</u>	<u>4,247,715</u>
Fund balances, ending	<u>\$1,881,306</u>	<u>\$390,715</u>	<u>\$1,734,737</u>	<u>\$763,409</u>	<u>\$4,770,167</u>

See accompanying notes to general purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO
COMBINED STATEMENT OF REVENUES, EXPENDITURES, ENCUMBRANCES,
AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL AND DEBT SERVICE FUNDS
YEAR ENDED JUNE 30, 2002**

	GENERAL FUND			DEBT SERVICE FUND		
	Budget	Actual	Variance Favorable (Unfavorable)	Budget	Actual	Variance Favorable (Unfavorable)
REVENUES						
Property taxes	\$2,182,472	\$2,601,347	\$418,875	\$552,779	\$984,785	\$432,006
Municipal license taxes	619,062	666,330	47,268			
Licenses and permits	249,413	386,623	137,210			
Intergovernmental	2,320,582	2,305,920	(14,662)			
Rent of property	22,835	28,450	5,615			
Fines and penalties	280	280	-			
Interest	20,770	46,952	26,182			
Miscellaneous	1,266,095	608,110	(657,985)			
Total revenues	<u>6,681,509</u>	<u>6,644,012</u>	<u>(37,497)</u>	<u>552,779</u>	<u>984,785</u>	<u>432,006</u>
EXPENDITURES AND ENCUMBRANCES:						
Current:						
Mayor and Municipal Assembly	918,604	904,092	14,512			
General government	2,518,218	2,232,898	285,320			
Public safety	134,281	132,486	1,795			
Public works	1,586,742	1,574,146	12,596			
Public health and sanitation	244,691	244,692	(1)			
Welfare	702,607	681,744	20,863			
Economic Development	32,708	32,148	560			
Recreation	263,760	257,964	5,796			
Principal retirement	29,000		29,000	300,000	329,000	(29,000)
Interest	8,320		8,320	252,779	156,236	96,543
Capital outlays	242,578	233,252	9,326			
Total expenditures and encumbrances	<u>6,681,509</u>	<u>6,293,422</u>	<u>388,087</u>	<u>552,779</u>	<u>485,236</u>	<u>67,543</u>
Excess (deficiency) of revenues over (under) expenditures and encumbrances		350,590	350,590		499,549	499,549
OTHER FINANCING SOURCES (USES):						
Bond Proceeds						
Operating transfer to other funds		(37,320)				
Operating transfer from other funds					37,320	
TOTAL OTHER FINANCING SOURCES (USES)		<u>(37,320)</u>			<u>37,320</u>	
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing sources (uses)		<u>313,270</u>			<u>536,869</u>	
Adjustment required under Generally Accepted Accounting Principles:						
GAAP adjustments to Revenues		(307,446)				
Current year encumbrances treated as current year expenditures for budgetary basis		783,699				
Prior year encumbrances paid during the current year		(253,464)				
Fund balances, beginning as restated		<u>1,345,247</u>			<u>1,197,868</u>	
Fund balance, ending		<u>\$1,881,306</u>			<u>1,734,737</u>	

See accompanying notes to general purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2002

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The **Municipality of Luquillo** (the Municipality) was established in 1787. The Municipality's governmental system consists of an executive and a legislative body. A Mayor and twelve members Municipal Assembly who are elected every four years through the Puerto Rico general elections govern it.

The Municipality provides the following services: public safety, public works, culture and recreation, health, urban development and welfare.

The Municipality's general-purpose financial statements are presented in accordance with generally accepted accounting principles (GAAP), as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. A summary of the Municipality's significant accounting policies follows:

A. Financial reporting entity:

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):

B. Basis of presentation:

The Municipality records its transactions in the fund types and account groups described below:

Governmental fund types:

Governmental funds are those through which most governmental functions are financed. The acquisition, use and balances of the Municipality's expendable financial resources and the related current 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 - is the general operating fund of the Municipality. It is used to account for all financial resources, except for those required to be accounted for in another fund.

Special Revenue - is used to account for the proceeds of specific revenue sources that are legally restricted to be expended for specific purposes.

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

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

Account groups:

The account groups are used to maintain accounting control and accountability of the Municipality's general fixed assets and long-term debt. The Municipality's account groups are:

General Fixed Assets - is used to account for all fixed assets of the Municipality.

General Long-term Debt - is used to account for all long-term debt obligations of the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):

C. Basis of accounting:

All governmental funds are accounted for using the modified accrual basis of accounting. Revenues are recognized when they become measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Revenues collected in advance of the fiscal year to which they apply are recorded as deferred revenues and recognized as revenues in the corresponding year. Expenditures are recorded when the liability is incurred, except for (1) interest on general long-term debt obligations which is recorded when due, and (2) accruals for vacation, sick leave, claims and judgments which are recorded in the general long-term debt account group.

In applying the susceptible to accrual concept to intergovernmental revenues, the legal and contractual requirements of the numerous individual programs are used as guidance. There are essentially two types of such revenues. In one situation, funds must be expended on the specific purpose or project before any amount is reimbursed to the Municipality; therefore, revenues are recognized based upon the expenditures recorded. In the other situation, funds are virtually unrestricted as to purpose of expenditure and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are recognized as revenues at the time of receipt or earlier if they meet the criteria of availability.

Licenses, permits, rent of property, fines, penalties and other miscellaneous revenues (except investment earnings) are recorded as revenues when received because they are generally not measurable until actually received.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):**

D. Reservations of fund balance:

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

Encumbrances - Represent future expenditures under purchases orders, contracts and other commitments issued for goods and services not received at year-end. Where the appropriations lapse at year-end these will be honored during subsequent year. Encumbrances constitute the equivalent of expenditures for budgetary purposes and, accordingly, are reported with expenditures in all budgetary basis statements.

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

E. Budgetary data:

In establishing the budgetary data presented in the general purpose financial statements, the Municipality follows these procedures, which are in accordance with the Municipal Law:

- Prior to May 31, the Major submits to the Municipal Assembly a proposed budget for the fiscal year commencing the following July 1. The proposed budget includes estimated expenditures and the means of financing them.
- The budget document is available for public inspection prior to its approval by the Municipal Assembly.
- Prior to July 1, the annual budget is legally enacted through passage of the annual appropriation ordinance.
- Subsequent to the enactment of the annual appropriation ordinance, the Municipal Assembly has the authority to make necessary adjustments to the budget. Adjustments made during the year are reflected in the budget information included in the general-purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):**

E. Budgetary data (continued):

The budget is prepared following the modified accrual basis of accounting, except for the encumbrances that are recorded as expenditures under the budgetary basis and as a reserve of funds balances under GAAP and for the interfund transactions that are not included in the budgetary basis.

The actual result of operations, presented in the Statement of Revenues, Expenditures, Encumbrances, and Changes in Fund Balances-Budget and Actual-General and Debt Service Funds, is in conformity with the budgetary accounting of the Municipality for a better comparison with the budget information.

The budget prepared for each of the special revenue funds is based on a program period, which is not necessarily the same as the Municipality's fiscal year. Accordingly, it is not practical to present an annual comparison of budget and actual for the special revenue funds.

F. Inventories:

The General Fund purchases office and printing supplies, gasoline, oil and other items. The cost of purchases is recorded as expenditure and, consequently, the inventory is not recorded in the general-purpose financial statements.

G. Property and equipment:

Property and equipment acquired are recorded as expenditures in the governmental funds and are capitalized at cost in the General Fixed Assets Account Group. Donated property and equipment are recorded at their estimated fair market value at the time they are received by the Municipality. No depreciation has been provided on property and equipment. Interest cost during the construction period is capitalized, when significant.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):**

H. Cash:

The Municipality's Director of Finance is responsible for investing available resources and is restricted by law to invest only in saving accounts and certificates of deposit with banks qualified as depositories of public funds by the Department of the Treasury of the Commonwealth of Puerto Rico. The Municipality maintains a cash pool that is available for use by all funds. Each fund type's portion of this pool is displayed on the combined balance sheet as Cash. All cash in banks at June 30, 2002 is insured by the Federal Deposit Insurance Corporation up to \$100,000, and by collateral held by the Treasury Department to its name. Interest earned from certificates of deposit and other short-term investments is recorded as revenue in the General Fund.

Cash with fiscal agent represents property tax collections retained by the Municipal Revenue Collection Center and Government Development Bank of the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, unused proceeds from bonds and notes issued for the acquisition or construction of permanent improvements and Federal grants resources.

I. Interfund transactions:

The Municipality has the following types of transactions among funds:

Operating transfers- Transfers that are reported when incurred as "Operating transfers from other fund" by the recipient fund and as "Operating transfers to other fund" by the disbursing fund.

Transfer of Expenditures (Reimbursements) - Reimbursement of expenditures made by one fund for another that are recorded as expenditures in the reimbursing fund and as reduction of expenditures in the reimbursed fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):**

J. Compensated absences:

Municipal employees are granted 30 days of vacation and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of 60 days and sick leave up to a maximum of 90 days. In the event of an employee resignation, the employee is reimbursed for accumulated vacation days up to the maximum allowed. Separation from employment prior to the use of all or part of the sick leave before 10 years of service terminates all rights for compensation.

The Municipality accrues a liability for compensated absences, which meet the following criteria:

1. The Municipality's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered.
2. The obligation relates to rights that vest or accumulate.
3. Payment of the compensation is probable.
4. The amount can be reasonably estimated.

In accordance with the above criteria and requirements as established by *GASB Number 16*, the Municipality has accrued a liability for compensated absences, which has been earned but not taken by municipal employees. This liability is presented in the general long-term debt account group because they will not be funded with available expendable financial resources at June 30, 2002.

K. Insurance:

The Municipality has insurance coverage for its public facilities, primarily to provide protection from catastrophic losses. The Secretary of the Treasury Department of the Commonwealth of Puerto Rico is the agent commissioned to place all of the Municipality's insurance coverage.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(CONTINUED):**

L. Total columns (memorandum only):

The total columns (memorandum only) are presented only to facilitate additional analysis. Consequently, amounts shown in total columns do not represent financial position or result of operations, in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation since interfund eliminations have not been made.

M. Use of estimates in the preparation of general purpose financial statements:

The preparation of general purpose financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures at the date of the general purpose financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

N. Claims and judgments:

The estimated amount of the liability for claims and judgments, if any, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund. The General Long-term Debt Account Group includes an amount estimated as a contingent liability or liabilities with a fixed or expected due date, which will require future available financial resources for its payment.

2. DUE TO OTHER GOVERNMENTAL ENTITIES:

The amounts due to other governmental entities in the General Fund include the following:

Retirement System Administration	\$ 6,390
Puerto Rico Aqueduct and Sewer Authority	5,116
General Services Administration	<u>2,543</u>
Total	<u>\$ 14,049</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

2. DUE TO OTHER GOVERNMENTAL ENTITIES (CONTINUED):

The Municipality reached agreements with other governmental entities for the payment of debts on a long-term basis. These liabilities are presented in the General Long-term Debt Account Group because they will not be funded with available expendable financial resources at June 30, 2002. The following is the balance of these accounts:

Department of Treasury (Social Security)	\$ 143,955
Department of Treasury (Property tax advances)	7,598
Municipal Revenue Collection Center (Property tax advances)	<u>739,900</u>
Total	<u>\$ 891,453</u>

3. PROPERTY TAXES:

The Municipal Revenue Collection Center ("CRIM") of the Commonwealth of Puerto Rico is responsible by law to assess, levy and collect real and personal property taxes. The tax on personal property is self-assessed by the taxpayer. The assessment, as of January 1 of each year, is made on a return, which must be filed, with the CRIM, together with the payment, by May 15 of each year. The tax on real property is assessed by the CRIM. The assessment is made as of January 1 of each year and is based on estimated current values of the property as of the year 1957.

Tax rates are 8.33% for real property and 6.33% for personal property of which 1.03% of both belongs to the Commonwealth of Puerto Rico. The Municipality's share is composed of the basic tax of 5.8% for real property and 3.8% for personal property, which is recorded in the General Fund, and the additional tax of 1.50% in both cases, which is restricted for debt service and retained by the CRIM for such purposes. To the extent that such taxes are informed and collected by the CRIM, they are recorded as revenue in the General Fund and in the Debt Service Fund.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the CRIM assumes payment of the basic tax to the Municipality, except for property assessed at less than \$3,500, for which no payment is made. Revenue related to the basic tax on exempt property is recorded in the general fund when payments are received from the CRIM.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

3. PROPERTY TAXES (CONTINUED):

Complete exemption from personal property taxes up to an assessment of \$50,000 is granted to retailers with an annual volume of net sales under \$150,000.

The CRIM advances to the municipality the estimated property tax collection for each fiscal year. Advances are repaid through actual collections from the taxpayers. The CRIM periodically informs the Municipality of the amounts collected and applied to outstanding advances. The property tax advanced by the CRIM during the year is recorded as property taxes revenues in the Municipality's General Fund. During the current year the advances were more than actual collections by \$163,877 according to CRIM final liquidation. Such amount was included as due to other Governmental Agencies in the General Long Term Debt Account Group at June 30, 2002. Also the Municipality has a \$583,621 Property Tax Advance debt balance from prior years (\$7,598 owed to Treasury Department and \$576,023 owed to CRIM) such balance was included as Due to Other Governmental Agencies in the General Long Term Debt Account Group because it will not be funded with available expendable financial resources at June 30, 2002.

4. MUNICIPAL LICENSE TAXES:

The municipal license tax is levied each year based on the prior year's gross revenues for all commercial and industrial organizations doing business in the Municipality, and which are not totally or partially exempt from this tax under the Industrial Incentives Acts of Puerto Rico. All taxpayers are required to file their declaration by April 15, of each year.

The tax rates are as follows:

Financial institutions	1.50%
Savings and loans associations	1.50%
Other organizations	0.50%

The tax may be paid in two equal semi-annual installments on July 15 and January 15 following the filing date. However, a discount of 5% is allowed for total payment received on or before April 15. Collections made prior to June 30 pertaining to the next fiscal year are recorded as deferred revenues.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

5. INTERGOVERNMENTAL:

Intergovernmental revenues consist mainly of payments from the Commonwealth of Puerto Rico and payments in lieu of taxes from certain quasi-public corporations, principally the Puerto Rico Electric Power Authority.

Grants and subsidies received from the Commonwealth of Puerto Rico include, among others, a general subsidy for capital improvements. Intergovernmental revenues are recorded in the General Fund, except for those related directly to capital improvements, which are recorded in the Capital Projects Fund.

6. DEBT SERVICE FUND:

Revenue for the Debt Service Fund consists mainly of the share of property taxes, which is designated for the debt service requirements of the bonds and notes obligations issued by the Municipality. The Government Development Bank pays principal and interest on these obligations.

7. GENERAL FIXED ASSETS:

A summary of changes in the General Fixed Assets Account Group is as follows:

Description	Balance July 1, 2001	Additions and adjustments	Retirements	Balance June 30, 2002
Buildings and Improvement	\$ 8,634,397	-	-	\$ 8,634,397
Equipment	4,516,884	\$ 219,150	(\$ 27,461)	4,708,573
Total	\$ 13,151,281	\$ 219,150	(\$ 27,461)	\$ 13,342,970

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

8. GENERAL OBLIGATION BONDS:

The general obligation bonds transactions for the year ended June 30, 2002 were as follows:

Balance at July 1, 2001	\$ 2,099,000
Principal retirements	<u>(129,000)</u>
Balance at June 30, 2002	<u>\$ 1,970,000</u>

General obligation bonds at June 30, 2002 are as follows:

Type of bonds	Maturity date	Original Amount	Range of Interest Rates	Balance at June 30, 2002
1984 Series	7-1-04	\$319,000	8.00%	\$ 75,000
1993 Series	7-1-12	\$2,015,000	5.00% - 8.00%	1,470,000
2000 Series	7-1-14	\$460,000	0.00% - 8.00%	<u>425,000</u>
Total general obligation bonds				<u>\$ 1,970,000</u>

The future annual requirements for the amortization of general obligations bonds outstanding as of June 30, 2002, are as follows:

Year ended June 30	Total
2003	\$ 145,000
2004	155,000
2005	130,000
2006	135,000
2007	145,000
Thereafter	<u>1,260,000</u>
Total	<u>\$ 1,970,000</u>

The Municipality is subject to certain laws of the Commonwealth of Puerto Rico, which limit the amount of bond debt to 10 percent of the assessed valuation of the property located in the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

9. NOTES PAYABLE:

The notes payable transactions for the year ended June 30, 2002 were as follows:

Balance at July 1, 2001	\$ 680,000
Payments during the current year	<u>(200,000)</u>
Balance at June 30, 2002	<u>\$ 480,000</u>

Notes payable at June 30, 2002 is as follows:

Description	Maturity Date	Original Amount	Range of Interest rates	Balance June 30, 2002
1993 Series	7-1-03	\$525,000	4.87% - 6.71%	\$ 205,000
2000 Series	7-1-04	\$425,000	0.00% - 8.00%	<u>275,000</u>
Total notes payable				<u><u>\$ 480,000</u></u>

The future annual requirements for the amortization of notes payable outstanding as of June 30, 2002, are as follows:

Year ended June 30	Total
2003	\$ 180,000
2004	200,000
2005	<u>100,000</u>
Total	<u><u>\$ 480,000</u></u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

10. RETIREMENT PLAN:

Defined Benefit Pension Plan

The Employees' Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (the "System") is the administrator of a cost sharing multiple-employer defined benefit public employee retirement system established by the Commonwealth of Puerto Rico. The System was created under the Act 447 approved on May 15, 1951, as amended. All regular employees of the Municipality hired before January 1, 2000 and less than 55 years of age at the date of employment became members of the System as a condition to their employment. No benefits are payable if the participant receives a refund of his/her accumulated contributions. The System also provides for death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature.

Under the System, the employees and employer portions are contributed, for which, the employee amount is withheld from salaries. Covered employees are required by Commonwealth statute to contribute 5.775% for the first \$550 of monthly gross salaries plus 8.275% for the excess of this amount, or on the alternative, 8.275% of monthly gross salaries. The Municipality contributes to the System 9.275% of the participating employee's gross salaries.

Pension benefits for employees that joined the system before April 1, 1990 are as follows:

<u>Years of Service</u>	<u>Participant Age</u>	<u>Pension Benefits</u>
30 or more	54 or less	65% of the average of the three years of highest salary during the employees' service period.
30 or more	55 or more	75% of the average of the three of highest salary during the employees' service period.

For participants who retire with less than 30 years of service the pension benefits is computed at the rate of 1-1/2% of their average compensation for each year of credited service for the first 20 years and 2% for each of credited service for the remaining years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

10. RETIREMENT PLAN (CONTINUED)

For those employees that joined the system after April 1, 1980 the pension benefits are as follows:

<u>Years of Service</u>	<u>Participant Age</u>	<u>Pension Benefits</u>
25 or more	Between 55 and 64	Computed at the rate of 1-1/2% of their average compensation for each year of credited service, with an actuarial reduction based on the actuarial guides adopted by the Board of Trustees.
10 or more	65 or more	Computed at the rate of 1-1/2% of their average compensation for each year-credited service.

For participants who retire with less than 25 years of service and the participant age are 64 or less the pension benefit is computed at the rate of 1-1/2% of their average compensation for each year of credited service.

Defined Contribution Plan

The Legislature of the Commonwealth enacted Act No. 305 on September 24, 1999, which amends Act No. 447 to establish, among other, a defined contribution saving plan program (the "Program") to be administered by the Retirement System. All regular employees hired for the first time on or after January 1, 2000 and former employees who participated in the defined benefit pension plan, received a refund of their contributions and are rehired on or after January 1, 2000 become members of the Program as a condition to their employment. In addition, employees who at December 14, 1999 were participants of the defined benefit pension plan, had the option, up to March 31, 2000, to irrevocably transfer their prior contributions to the defined benefit pension plan plus interest thereon to the Program.

Act No. 305 requires employees to contribute 8.275% of their monthly gross salary to the Program. Employees may elect to increase their contribution up to 10% of their monthly gross salary. Employee contributions are credited to his/her individual account established under the Program. Participants have three options to invest their contributions to the Program. Investment income is credited to the participant's account semi-annually.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

10. RETIREMENT PLAN (CONTINUED):

The Municipality is required by the Act No. 305 to contribute 9.275% of the participant's gross salary. The System will use these contributions to increase its asset level and reduce the unfounded status of the defined benefits pension plan.

Upon retirement, the balance in the participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life and 50% of such benefit to the participant spouse in case of the participant death. Participants with balance of \$10,000 or less at retirement will receive a lump-sum payment. In case of death, the balance in the participant's account will be paid in a lump sum to his/her beneficiaries. Participants have the option of a lump sum or purchasing an annuity contract in case of permanent disability.

Total Municipality contributions to the above-mentioned plans during the year ended June 30, 2002 recorded as pension expenditures were approximately **\$202,000**. This amount represents 100% of the required contribution for the fiscal year ended June 30, 2002.

The amount of the total pension benefit obligation is based on a standardized measurement established by GASB Number 27, *Accounting for Pensions by State and Local Governmental Employers*. The standardized measurement is the actuarial present value of credited projected benefits. This pension valuation method reflects the present value of estimated pension benefits that will be paid in future years as a result of employee's services performed to date and is adjusted for the effects of projected salary increases. The significant actuarial assumptions used to determine the standardized measure of the pension benefit obligation are summarized below:

- * The present value of the future pension payments was computed by using a discount rate of 8.5%. The discount rate is equal to the estimated long-term rate of return on current and future investments of the pension plan.
- * Future pension payments reflect an assumption of 5% salary increase.

The measure is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among other public retirement systems. The measure is independent of the actuarial funding method used to determine contributions to the plan.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

10. RETIREMENT PLAN (CONTINUED):

The membership of retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits, but not yet receiving benefits, and active employees and the distribution of active employees between vested and nonvested is not readily available. Contributions in 2001 and prior years were made based on percentages established by the law. Such percentage has not been based on actuarial studies, as required by generally accepted accounting principles. An actuarial compilation of the annual contribution applicable to the Municipality has not been prepared. Accordingly, the accounts by which the actual contributions differ from the required actuarial contributions are not known.

The ten-year historical trend information is available in the separately issued audited financial statements of the Retirement System.

11. INTERFUND TRANSACTIONS:

Due from/to other funds

Interfund receivables and payables represent temporary loans between the funds.

Operating transfers

Operating transfers represent transfers between funds to specific purposes designated by the management.

12. COMMITMENTS AND CONTINGENCIES:

A. Federal grants:

The Municipality participates in a number of Federal Financial Assistance Programs. These programs are subject to financial and compliance audits. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the Municipality expects such amounts, if any, not to be material.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

12. COMMITMENTS AND CONTINGENCIES (CONTINUED):

B. Claims and lawsuits:

The Municipality is a defendant in legal matters that arise in the ordinary course of the Municipality's activities. With respect to pending and threatened litigation, the Municipality has reported liabilities of \$27,500 in the General Long Term Debt Account Group for anticipated unfavorable judgments. The amount presented in the general long term debt group of account represents the amount of estimated as probable liability, which will require future available financial resources for its payments. The administration believes that the ultimate liability, if any, would not be significant.

13. BEGINNING FUND BALANCES RESTATEMENT:

The beginning Fund Balances for General and Debt Service Funds have been restated by accounting errors detected during the fiscal year that affect the Fund Equity section of those Governmental Funds, as follows:

<u>Description</u>	<u>General</u>	<u>Debt Service</u>
Beginning Fund Balances at July 1, 2001	\$1,037,801	\$1,457,085
Account Receivable from CRIM related to fiscal year 2000-2001 Final Liquidation	307,446	
Account Receivable from CRIM related to 1999-2000 CAE final liquidation		180,281
Account Payable to CRIM related to 2000-2001 CAE final liquidation		(439,498)
Beginning Fund Balances at July 1, 2001, as restated	<u>\$1,345,247</u>	<u>1,197,868</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2002

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF AGRICULTURE:			
Direct Program:			
Nutrition Program for the Elderly	10.570		\$ <u>29,355</u>
Total U.S. Department of Agriculture			<u>29,355</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Section 8 Housing Choice Vouchers	14.871		438,161
Pass-through the Commonwealth of Puerto Rico - Office of the Commissioner of Municipal Affairs:			
Community Development Block Grants - State's Program	14.228	97-FD-41 98-FD-41 99-FD-41 00-FD-41 01-FD-41	<u>349,432</u>
Total U.S. Department of Housing and Urban Development			<u>787,593</u>
U.S DEPARTMENT OF JUSTICE:			
Pass-through the Commonwealth of Puerto Rico - Office of the Governor (Youth Office):			
Title V - Delinquency Prevention Program	16.548	00-JP-FX-0072	<u>12,725</u>
Total U.S. Department of Justice			<u>12,725</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S DEPARTMENT OF TRANSPORTATION:			
Pass-through the Commonwealth of Puerto Rico Transit Safety Commission:			
Incentive Grant	20.601	Not Available	1,600
Total U.S. Department of Transportation			1,600
U.S FEDERAL EMERGENCY MANAGEMENT AGENCY:			
Pass-through the Commonwealth of Puerto Rico - Governor Authorized Representative (GAR):			
Public Assistance Grants	83.544	1247-DR-PR	5,068
Hazard Mitigation Grant	83.548	1247-DR-PR	126,008
Total U.S. Federal Emergency Management Agency			131,076
U.S DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico Governor's Office (Elderly Office):			
Special Programs for Aging - Title III, Part B - Grant for Supportive Services and Senior Centers	93.044	Not Available	114,575

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
Pass-through the Commonwealth of Puerto Rico Administration for Children and Families: Child Care and Development Block Grant	93.575	Not available	<u>114,375</u>
Total U.S. Department of Health and Human Services			<u>228,950</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 1,191,299</u>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2002

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the **Municipality of Luquillo** and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the general-purpose financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue Fund in the Municipality's general-purpose financial statements. The reconciliation between the expenditures in the general-purpose financial statements and the expenditures in the Schedule of Expenditures of Federal Awards is as follows:

<u>Description</u>	<u>Special Revenue</u>
Per Schedule of Expenditures of Federal Awards	\$ 1,191,299
Non federal programs expenditures	444,985
Total expenditures in the general purpose financial Statements	<u>\$ 1,636,284</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

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

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Luquillo
Luquillo, Puerto Rico**

We have audited the general purpose financial statements of the **Municipality of Luquillo** as of and for the year ended June 30, 2002, and have issued our report thereon dated November 22, 2002, which was qualified because we were unable to audit the fixed assets of the general fixed assets account group. Except as discussed in the preceding sentence, 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 the **Municipality of Luquillo's** general purpose financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of general purpose 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Luquillo's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting that, in our judgment, could adversely affect **Municipality of Luquillo's** ability to record, process, summarize, and report financial data consistent with the assertions of management in the general purpose financial statements. The reportable conditions are described in the accompanying schedule of findings and questioned costs items 02-01 through 02-03.

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

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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose reportable conditions that are also considered to be material weaknesses. However, we believe item **02-01** of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management of the **Municipality of Luquillo** in a separate letter dated November 22, 2002.

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.



LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
November 22, 2002

Stamp No. 1854011 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.





López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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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 the Municipal Legislature
Municipality of Luquillo
Luquillo, Puerto Rico**

Compliance

We have audited the compliance of the **Municipality of Luquillo** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2002. The **Municipality of Luquillo's** major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the **Municipality of Luquillo's** management. Our responsibility is to express an opinion on the **Municipality of Luquillo'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 the *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **Municipality of Luquillo'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 on the **Municipality of Luquillo's** compliance with those requirements.

As described in items **02-12** through **02-20** in the accompanying schedule of findings and questioned costs, the **Municipality of Luquillo** did not comply with requirements regarding Eligibility for Individuals, Reporting and Special Test that are applicable to its Section 8 Housing Choice Voucher Program. Compliance with such requirements is necessary, in our opinion, for the **Municipality of Luquillo** to comply with requirements applicable to that program.

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 (CONTINUED)

In our opinion, except for the noncompliance described in the preceding paragraph, the **Municipality of Luquillo** 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, 2002. The results of our auditing procedures also disclosed other 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, **02-04** through **02-11**.

Internal Control Over Compliance

The management of the **Municipality of Luquillo** 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 Luquillo's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the **Municipality of Luquillo's** ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items **02-04** through **02-20**.

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 on the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weakness. However, of the reportable conditions described above, we consider items **02-04**, **02-06**, **02-09** and **02-11** through **02-20** to be material weaknesses. We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Luquillo** in a separate letter dated February 18, 2003.



**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(CONTINUED)**

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

Lopez-Vega CPA PSC
LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
February 18, 2003

Stamp No. 1854012 of the Puerto Rico
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was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2002

Section I – Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued:	Qualified		
Internal control over financial reporting:			
Material weakness identified?	Yes	X	No
Reportable conditions identified not considered to be material weaknesses?	Yes	X	None reported
Noncompliance material to financial statements noted?	Yes		No X

Federal awards

Internal Control over major programs:			
Material weakness identified?	Yes	X	No
Reportable conditions identified not considered to be material weaknesses?	Yes	X	None reported
Type of auditors’ report issued on compliance for major programs:	Unqualified, except Qualified for Section 8 Housing Choice Voucher (CFDA No. 14.871)		
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes	X	No

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
14.228	Community Development Block Grant – State’s Program
14.871	Section 8 Housing Choice Voucher

Dollar threshold used to distinguish between Type A and Type B programs	\$ 300,000		
Auditee qualified as low-risk auditee?	Yes		No X

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II – Financial Statements Findings

Finding Reference **02-01**

Requirement **Fixed\Capital Assets and Expenditures – Subsidiary Ledger**

Statement of Condition During our examination of Municipality's property records and reports we noted the following deficiencies: the balance in the Property Subsidiary Ledger does not reconcile with the ending balances reported in the audited financial statements; there is no adequate internal control procedures to assure the proper valuation and timeliness of recognition of real and personal property in the Property Subsidiary Ledger; Construction in Progress account were not maintained in the General Ledger and Property Subsidiary Ledger.

Criteria Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain updated property accounting records. Also, the federal regulations establish that a financial management system shall provide for effective control and accountability for all funds, property and other assets.

Cause of Condition There is no internal control procedures implemented to assure the completeness of the property records and reports.

Effect of Condition The Municipality is not in compliance with Chapter IX, Article 9.002 of the State Act Number 81 and with the federal regulations.

Recommendation We recommend that the Municipality should implement procedures in order to assure the proper valuation and timeliness of recognition of real and personal property as well as Construction in Progress in the Property Subsidiary Ledger in a manner that it provides updated and complete financial information.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II - Financial Statements Findings

Finding Reference **02-02**

Requirement **Financial Reporting - Accounting Records**

Statement of Condition During our examination of the Municipality's accounting system we noted that it does not summarize the transactions in a formal General Ledger in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal funds) and Account Groups.

Criteria Chapter VIII, Article 8.010 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain an effective and updated accounting system.

Cause of Condition The Municipality did not establish effective internal control over the transactions recorded on its accounting records. Also, the accounting data is not summarized in the form of a double-entry general ledger record.

Effect of Condition The Municipality's accounting system did not provide updated and complete financial information that present the financial position, the result of operations and the change in fund balances. Such information is necessary to take management decisions.

Recommendation We recommend that the Municipality should implement the necessary internal controls and procedures in order to maintain an accounting system that contains information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, expenditures, interfund transactions, etc.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II - Financial Statements Findings

Finding Reference **02-03**

Requirement **Expenditures for Goods and Services and Account Payables -
Purchasing and Receiving**

Statement of Condition During our examination of the Municipality's procedures related to the purchasing and receiving process we examined forty two (42) disbursement vouchers and we noted the following situations:

- a. Five (5) disbursement vouchers did not have all supporting documents stamped as paid.
- b. On fourteen (14) disbursement vouchers there was no evidence of invoices.
- c. On seventeen (17) disbursement vouchers there was no evidence of receiving report or the certification of the Municipality's employee who received the goods or services.
- d. Four (4) cancelled checks were not available for our examination.
- e. On thirteen (13) disbursement vouchers there was no evidence that supports if the purchase order were issued before the receiving of goods or services.
- f. On five (5) disbursement vouchers there was no evidence that the Municipality obtained at least three quotations or realized formal bids for these purchases. Also, in one (1) disbursement voucher the Municipality did not select the lowest quotation.
- g. On thirteen (13) disbursement vouchers there was no evidence of the signature of the employee who asked for the quotations and there is no evidence of the signature of the employee who authorized the purchase of goods or services.

Other conditions related with the disbursements vouchers of the Community Development Block Grants - State's Program and with the Section 8 Housing Choice Voucher Program, were included on the Finding Number 02-04 and Finding Number 02-10.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II - Financial Statements Findings

Finding Reference **02-03 (continued)**

Criteria The Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establish in Chapter four (4) that the Finance Director will be responsible to account and to prepare disbursements through documents duly prepared and certified, including sufficient evidential matter to support the transactions. Chapter eight (8) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establishes the procedures related to the formal bids or quotations for the purchase of goods or services. Also, the Article 10.007 of State Act Number 81 of August 30, 1991 establishes procedures to request and obtain bids and quotation from the suppliers.

Cause of Condition The Municipality did not establish effective internal control to assure that all transactions include all the required documentation. Also, the Municipality did not maintained effective internal controls to assure an adequate procurement process for all purchase of goods or services.

Effect of Condition The Municipality is not in compliance with Revised Regulations on Basic Standards for the Municipalities of Puerto Rico and with the State Act Number 81 of August 30, 1991.

Recommendation We recommend that the Municipality should improve its internal control and procedures in order to assure that all disbursement vouchers contain all supporting documents before the payment is made. Also, we recommend that the Municipality should improve its procedures to assure that at least three quotations be requested for all purchases of goods or services that do not exceed \$10,000 and construction contracts that do not exceed \$40,000 or realize formal bids for purchases that exceed these limits.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-04
Program	Community Development Block Grants - State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico - Office of Commissioner of Municipal Affairs
Requirement	Allowable Cost - Cost Principles
Statement of Condition	<p>During our disbursement test of the Community Development Block Grant - State's Program we noted the following situations:</p> <ul style="list-style-type: none">a. Five (5) cancelled checks were not available for our examination.b. On nine (9) disbursement vouchers the purchase orders were prepared after the receiving of the goods or services.c. In one (1) payment the supplier included in the invoice a change in the scope of work stated in the original contract. The original contract included a provision for the preparation of an Environmental Study but the invoice included a change for a Traffic Study. We could not obtain evidence of the change order signed by the Municipality and the supplier. The invoice amount was \$15,000.
Criteria	Code of Federal Regulations 24, Subpart C, Part 85.20 (b) (6) states that accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and sub grant award documents and others.
Cause of Condition	Municipality did not maintain adequate controls to assure that all disbursements made have all the necessary supporting documents and were realized for allowable costs.
Effect of Condition	Municipality is not in compliance with Code of Federal Regulation, Subpart C, 24 CFR 85.20 (b) (6), provisions regarding allowable cost.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-04 (continued)**

Recommendation We recommend that the Municipality should strength its procedures to assure that all disbursements vouchers contain all supporting documents and approval signatures before the related payments are made.

Questioned Cost \$15,000

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-05
Program	Community Development Block Grant - State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through State - Office of Commissioner of Municipal Affairs (OCAM)
Requirement	Davis-Bacon Act
Statement of Condition	<p>During our Davis-Bacon Act test for the construction project (00-FD-41-005), we noted that the Municipality did not apply adequately the monitoring system developed to ensure contractors compliance with payment of prevailing wages rates to employees.</p> <p>We noted the following situations: contractor's and subcontractor's laborers interviews were not made; contractor weekly payrolls were not requested during activity of construction project to be reviewed by the municipal employee responsible of applying monitoring procedures.</p>
Criteria	Davis-Bacon Act, as amended (40 USC 276A-276A-5), Subpart K, 24 CFR 570.603.
Cause of Condition	Municipality did not apply all monitoring system procedures developed to test applicable contractors with respect to payment of prevailing wages.
Effect of Condition	Municipality is not in compliance with Davis-Bacon Act, as amended (40 USC 276A-276A-5), Subpart K, 24, CFR 570.603

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-05 (continued)**

Recommendation We recommend management to follow monitoring system procedures developed, including obtaining contractor's and subcontractor's weekly payrolls to be reviewed on a weekly basis by the responsible municipal employee, and interview contractor's and subcontractor's laborers periodically (up to ten percent (10%) of the workers on long term projects) to establish the degree of compliance and the nature and extend of violations, if any.

Questioned Costs None

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-06
Program	Community Development Block Grant - State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through State - Office of Commissioner of Municipal Affairs (OCAM)
Requirement	Equipment and Real Property Management
Statement of Condition	Section II - Financial Statements Findings - Finding Reference 02-01

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-07
Program	Community Development Block Grants - State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico - Office of Commissioner of Municipal Affairs
Requirement	Procurement
Statement of Condition	During our disbursement test of the Community Development Block Grant - State's Program we did not find evidence that the Municipality requested proposals for the adjudgment of a contract for professional services.
Criteria	Code of Federal Regulations 24, Subpart I, 570.489 (g) states that when procuring property or services to be paid for in whole or in part with CDBG funds, the state shall follow its procurements policies and procedures. The state shall establish requirements for procurement policies and procedures for units of general local government, based on full and open competition.
Cause of Condition	The Municipality did not maintain effective controls to assure an adequate procurement process for all purchase of goods or services.
Effect of Condition	Municipality is not in compliance with Code of Federal Regulation, Subpart I, 24 CFR 570.489 (g), provisions regarding procurement process.
Recommendation	We recommend that the Municipality should improve its procedures to assure that proposals should be requested for the acquisition of professional services.
Questioned Cost	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-08**

Program **Community Development Block Grants – State’s Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through the Commonwealth of Puerto Rico – Office of Commissioner of Municipal Affairs**

Requirement **Reporting**

Statement of Condition During our audit we noted that the Financial Management Quarterly Reports for the quarterly from July 1, 2001 through September 30, 2001, from October 1, 2001 through December 31, 2001, and from January 1, 2002 through March 31, 2002 were not submitted to the Pass Through Agency during the thirty (30) days period stated in the grant agreement.

Criteria OMB Common Rules, Subpart C, Section 85.20, states that the grantee must maintain internal control procedures that permits proper tracing of funds to the accounting records. Also, it requires accurate, current and complete disclosure of financial results.

Cause of Condition The Municipality did not maintain an adequate internal control to assure that the Financial Management Quarterly Reports are accurately prepared in order to assure that the information reported is in accordance with the accounting records.

Effect of Condition The Municipality is not in compliance with OMB Common Rules, Subpart C, and Section 85.20.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-08 (continued)**

Recommendation We recommend that the Municipality should implement procedures in order to assure that all financial and programmatic reports are submitted on time to the agencies and prepared in accordance with the required accounting basis.

Questioned Costs None

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-09
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Financial Administration - Standard for Financial Management System
Statement of Condition	During our audit we noted that the Municipality did not maintain for the Section 8 Housing Choice Vouchers Program a reliable set of accounting records that present the financial position of the program, the results of operations and changes in fund balance.
Criteria	<p>Code of Federal Regulations 24, Subpart C, Part 85.20 (b) (2) states that the grantees and sub grantees must maintain records, which adequately identify the source and application of funds, provided for financially-assisted activities. These records must contain information pertaining to grant or sub grant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.</p> <p>The Housing Assistance Payments Program Accounting Handbook states the minimum HUD accounting requirements with respect to Housing Assistance Payments Program Projects under annual contribution contracts.</p>
Cause of Condition	Municipality did not maintain adequate controls and accounting records to assure the accountability of all Federal transactions in accordance with Federal regulations. This situation may cause the non-compliance with certain regulations like allowable costs or allowable activities and financial reporting preparations.
Effect of Condition	Municipality is not in compliance with Code of Federal Regulation 24, Subpart C, Part 85.20 (b) (2) and, with the Housing Assistance Payments Program Accounting Handbook.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-09 (continued)**

Recommendation We recommend that the Municipality should implement controls and procedures in order to assure the accountability of all financial transactions as required by the federal regulations.

Questioned Cost None.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-10
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Allowable Cost - Cost Principles
Statement of Condition	<p>During our disbursement test on the Section 8 Housing Choice Vouchers Program transactions we noted the following situations:</p> <ul style="list-style-type: none">a. In two (2) disbursement vouchers there was no evidence of invoices.b. In three (3) disbursement vouchers there was no evidence of receiving report or the certification of the Municipality's employee who received the goods or services.c. In three (3) disbursement vouchers the purchase order was prepared after the receiving of the good or services. Also, in one (1) disbursement voucher there was no evidence that showed us if the purchase order was prepared before the receiving of the goods or services.
Criteria	Code of Federal Regulations 24, Subpart C, Part 85.20 (b) (6) states that accounting records must be supported by such source documentation as cancelled checks, paid bills, payrolls, time and attendance records, contract and sub grant award documents and others.
Cause of Condition	Municipality did not maintain adequate controls to assure that all disbursements made have all the necessary supporting documents and were realized for allowable costs.
Effect of Condition	Municipality is not in compliance with Code of Federal Regulation, Subpart C, 24 CFR 85.20 (b) (6), provisions regarding allowable cost.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-10 (continued)**

Recommendation We recommend that the Municipality should strength its procedures to assure that all disbursements vouchers contain all supporting documents and approval signatures before the related payments are made.

Questioned Cost None.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-11
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Activities Allowed or Unallowed
Statement of Condition	<p>We selected for examination a sample of twenty five (25) participant's files and noted the following situations:</p> <ul style="list-style-type: none">a. Two (2) participant files were not available for our examination.b. In eighth (8) participant files we noted that the PHA did not actualized the contracts with the owner to make HAPs on behalf of the Family.
Criteria	<p>Code of Federal Regulations 24, Subpart D, Section 982.158 (a) states that the PHA must maintain complete and accurate accounts and other records for the program in accordance with HUD requirements, in a manner that permits a speedy and effective audit. The records must be in the form required by HUD, including requirements governing computerized or electronic forms or record-keeping. Also, the CFR 24, Subpart D, Section 982.158 (d) states the documents and reports that the PHA must keep during the term of each assisted lease, and for at least three years thereafter.</p> <p>The Code of Federal Regulations 24, Subpart D, Section 982.1 (a)(2) states that if the PHA approves a family's unit and determines that the rent is reasonable, the PHA contracts with the owner to make HAPs on behalf of the family.</p>
Cause of Condition	<p>The PHA did not maintain appropriate controls and procedures to assure that all documents, records and files were maintained according with the federal regulations. Also, the PHA did not maintain appropriate controls and procedures in order to prepare or actualize contracts with the owners to make HAPs on behalf of the family.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-11 (continued)**

Effect of Condition The Municipality is not in compliance with the Code of Federal Regulations 24, Subpart D, Section 982.158 (a) and (d). Also, the Municipality is not in compliance with the Code of Federal Regulations 24, Subpart D, Section 982.1 (a)(2).

Recommendation We recommend that the Municipality should implement and design procedures in order to assure that the documents and records were properly maintained. Also, the Municipality should strength its procedures in order to assure that the contracts were actualized and prepared every time the PHA approves a family's unit.

Questioned Costs None.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-12**

Program **Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development**

Requirement **Eligibility of individuals**

Statement of Condition We performed an eligibility test and examined twenty three (23) participant's files. The following summarizes the situations found:

- a. In sixteen (16) participant files the release form to allow the PHA to obtain information from third parties was obtained by the Municipality in the admission process fiscal years prior to the fiscal year 2001-2002. The Municipality did not obtain a new release form during the fiscal year 2001-2002 during the re-examination or interim re-examination process. Also, the release forms obtained by the Municipality did not contain the minimum information required by the federal regulations.
- b. Three (3) participant files did not include a release form to allow the PHA to obtain information from third parties.
- c. In three (3) participant files the release form to allow the PHA to obtain information from third parties did not contain the minimum information required by the federal regulations.
- d. Seven (7) participant files did not contain a release form to allow the PHA to obtain information from third parties, signed by the head of household spouse or by any members of the family composition who is at least eighteen (18) years of age.
- e. In twenty two (22) participant files there was no evidence that the PHA provide to the assistance applicants and to the participants in the annual income recertification a "Privacy Act Notice".

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-12 (continued)**

- f. In sixteen (16) participant files the PHA did not obtain during the fiscal year 2001-2002 actualized evidence of reported family annual income, expenses related to deductions from annual income, the value of assets, and evidence of family compositions.
- g. In four (4) participant files the PHA did not obtain during the admission or re-examination process, complete evidence to support family annual income, expenses related to deductions to annual income, and family composition.

Criteria Code of Federal Regulations 24, Sections 5.230, and 982.516 states that as a condition of admission or continued occupancy, require the tenant and other family members to provide necessary information, documentation and releases for the PHA to verify income eligibility.

Code of Federal Regulations 24, Subpart B, Section 5.212 (b) states that all assistance applicants shall be provided with a Privacy Act Notice at the time of application. All participants shall be provided with a Privacy Act Notice at each annual income recertification.

Cause of Condition The Federal Program Department does not maintain adequate monitoring system to assure that the participant files include all required documentation and releases required by federal agencies.

Effect of Condition The Municipality is not in compliance with Code of Federal Regulations 24, Sections 5.212 (b), 5.230 and 982.516.

Recommendation We recommend the Program to establish monitoring procedures to assure that the participant's files include all documentation required by federal agencies.

Questioned Costs None.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-13
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Eligibility of Individuals
Statement of Condition	<p>During our verification of twenty three (23) participant files we noted the following exceptions related to the Housing Assistance Payment Calculations:</p> <ul style="list-style-type: none">a. In nine teen (19) participant files the PHA did not realize a family income and composition reexamination at least once every twelve (12) months. During the fiscal year 2001-2002 the PHA performed re-examinations or interim re-examinations but did not require the participants actualized evidence to support these examinations.b. We noted that in sixteen (16) participant files the PHA determined the Housing Assistance Payment for the fiscal year 2001-2002 using supporting evidence obtained on the admissions or re-examination process of prior years.c. We noted that in four (4) participant files the PHA determined the Housing Assistance Payment for the fiscal year 2001-2002 using incomplete supporting evidence of family annual income, evidence of expenses related to deductions from annual income, and evidence of family composition.
Criteria	<p>Code of Federal Regulations 24, Sections 982.201, 982.515 and 982.516 establish income eligibility and tenant's rent payment calculation requirements. Also, requires the PHA to reexamine family income and composition at least once every twelve months and adjust the tenant rent and housing assistance payment as necessary.</p>
Cause of Condition	<p>The Federal Program Department did not perform adequate monitoring procedures to assure that all HAPs payments are duly computed by the program staff.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-13 (continued)
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Sections 982.201, 982.515 and 982.516.
Recommendation	We recommend the Municipality to perform monitoring procedures to assure the HAPs are duly computed as required by the Federal Regulations. Also, we recommend the Municipality to perform monitoring procedures to assure that a reexamination of family income and composition will be made at least once every twelve months and will adjust the tenant rent and housing assistance payment as necessary.
Questioned Costs	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-14
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Reporting - Financial Reporting
Statement of Condition	During our reporting test we noted that the Municipality did not maintain a reliable set of accounting records for the Section 8 Housing Choice Voucher Program, thus, we could not obtain evidence that assured us that the HUD-52681, Voucher for Payment of Annual Contributions and Operating Statements (OMB No. 2577-0169) was prepared according with Federal Regulation. Also, we noted some mathematical errors in the preparation of this report.
Criteria	Code of Federal Regulation 24, Subpart C, Section 85.20, states that the grantee must maintain internal control procedures that permits proper tracing of fund to accounting records. Also, it requires accurate, current and complete disclosure of financial results. The Housing Assistance Payments Program Accounting Handbook states the minimum HUD accounting requirements with respect to Housing Assistance Payments Program Projects under annual contribution contracts.
Cause of Condition	Municipality did not maintain adequate controls and accounting records to assure that the financial and programmatic reports were prepared according to Federal and State Regulations.
Effect of Condition	Municipality is not in compliance with Code of Federal Regulations, Subpart C, Section 85.20, provisions regarding financial reporting.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-14 (continued)**

Recommendation We recommend the Municipality should implement controls and procedures in order to assure accurate accounting records are maintained and current and complete disclosure of financial results are presented in the financial reports. Also, we recommend that the Municipality should implement procedures in order to assure that all financial and programmatic reports are submitted on time to the agencies and are prepared in accordance with the required accounting basis.

Questioned Cost None

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-15
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Reporting - Performance Reporting
Statement of Condition	The Municipality SEMAP Report for the fiscal year ended June 30, 2002 was not completed by the Municipality in all of its parts. Also, the Municipality included an affirmative answer in the majority of the performance indicators, nevertheless the results of our test shows exceptions related to the compliance with the majority of those requirements.
Criteria	Code of Federal Regulations 24, CFR, Section 985.3 and 982.101 states that HUD 52648, SEMAP certification and the Addendum for Reporting Data for Deconcentration Bonus Indicator for PHAs with jurisdiction in metropolitan FMR areas should be submitted to HUD within sixty (60) calendar days after the end of its fiscal year. HUD will realize on site visits and verify the independent auditor's annual reports to assure compliance with this requirement.
Cause of Condition	The Municipality does not maintain adequate monitoring procedures to assure the compliance with the submission and with the answers detailed in the SEMAP Report.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Section 985.3 and 982.101.
Recommendation	We recommend the Municipality to improve its internal controls and monitoring procedures to assure that the program complies with federal regulations.
Questioned Costs	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-16
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Reporting - Special Reporting
Statement of Condition	We noted that the form HUD 50058, Family Report (OMB No. 2577-0083) was not submitted electronically to HUD during the fiscal year 2001-2002.
Criteria	Code of Federal Regulations 24, Section 908 and 982.158 requires the PHA to submit the form HUD-50058, Family Report, electronically to HUD each time the PHA completes an admission, annual reexamination, interim reexamination, portability move-in, or other change or unit for a family. The PHA must also submit the Family Report when a family ends participation in the program or moves out to the PHA's jurisdiction under portability.
Cause of Condition	The Federal Program Department did not perform adequate monitoring procedures to assure that the submissions of the Family Reports were performed on a timely basis.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Section 908 and 982.158.
Recommendation	We recommend the Municipality to strength it's procedures in order to assure that the form HUD-50058, Family Report, was submitted electronically to HUD each time the PHA completes an admission, annual reexamination, interim reexamination, portability move-in, portability move-out, and when a family end participation in the program.
Questioned Costs	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-17
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Selection from the Section 8 Waiting List
Statement of Condition	During our waiting list test we could not obtain evidence that the Municipality maintained an adequate waiting list. We couldn't obtain evidence to verify how participants were selected from the top of the waiting list.
Criteria	Code of Federal Regulations 24, Section 982.54 (d), and 982.201 through 982.207 states the waiting list procedures. The PHA must have written policies in its HCVP administrative plan for selecting applicants from the waiting list and PHA documentation must show that the PHA follows these policies when selecting applicants for admission from the waiting list. Except for special admission applicants, all families admitted to the program must be selected from the waiting list. Selection from the waiting list generally occurs when the PHA notifies a family whose name reaches the top of the waiting list to come in to verify eligibility for admission.
Cause of Condition	The Federal Program did not perform adequate monitoring procedures to assure the existence and maintenance of a waiting list and to assure that participants were selected from the top of the waiting list.
Effect of Condition	The Municipality is no in compliance with 24 CFR sections 982.54 (d) and 982.201 through 982.207. .

COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 02-17 (Continued)

Recommendation We recommend to the management to create a waiting list that contains all requirements of the federal regulations. Also, we recommend management to create and maintain a clear set of participant selection procedures to assure that except for the special admissions, all families admitted to the program must be selected from the waiting list.

Questioned Costs None.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-18
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test - Reasonable Rent
Statement of Condition	During our verification of twenty three (23) participant files we noted that the determination of reasonable rent (reasonable rent certification) was not available for our examination in all files.
Criteria	Code of Federal Regulations 24, Sections 982.54 (d)(15), 982.158 (f) (7) and 982.507 states that the PHA must determine reasonable rent at the time of the initial leasing and must maintain records to document the basis for the determination that the rent paid to the owner is reasonable. Also, the PHA must determine reasonable rent during the term of the contract: (a) before any increase in the rent to owner; and (b) at the HAP contract anniversary if there is a five percent decrease in the published Fair Market Rent in effect 60 days before the HAP contract anniversary.
Cause of Condition	The Federal Program Department did not maintain adequate procedures to determine if the rent paid to the owners was reasonable and did not maintain procedures to document the basis for the determination.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Sections 982.54 (d) (15), 982.158 (f) (7) and 982.507.
Recommendation	We recommend that the Federal Program Department must establish adequate controls to assure that the rent paid to the owners was reasonable and that appropriate documentation of the determination of reasonable rent is maintained in participant's files.
Questioned Costs	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-19
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test - Utility Allowance Schedule
Statement of Condition	The Municipality did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2002. There is no evidence of the last time that the Utility Allowance Schedule was actualized.
Criteria	Code of Federal Regulations, 24 CFR Section 982.517 states that the Municipality must maintain an up-to-date utility allowance schedule. The Municipality must review utility rate data for each utility category each year and must adjust its allowance schedule if there has been a rate change of ten percent or more for a utility category or fuel type since the last time utility allowance was revised.
Cause of Condition	The Municipality did not follow the procedures established to review utility rate data each year.
Effect of Condition	The Municipality is no in compliance with Code of Federal Regulations, 24 CFR Section 982.517.
Recommendation	The Municipality should evaluate utility allowance rate each year as established in the federal regulations.
Questioned Costs	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-20
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Housing Quality Standards Inspections and Housing Quality Standards Enforcement
Statement of Condition	<p>During our examination of twenty three (23) participant files we noted the following situations:</p> <ul style="list-style-type: none">a. On thirteen (13) participant files there was no evidence that the Municipality performed a Housing Quality Standard Inspection during the fiscal year 2001-2002.b. On two (2) participants files there was no evidence that the Municipality performed a Housing Quality Standard Inspection to a newly leased unit.c. In our examination of twenty three (23) participant files there was no evidence of a quality control re-inspections performed and documented by a reasonable official. The Program Coordinator represented to us that during the fiscal year 2001-2002 the Municipality did not perform quality control re-inspections.d. On three (3) participant files the Municipality did not document the time frame that the owner or the family had to correct the deficiencies noted on the unit inspection. Also, there was no evidence that the Municipality followed up the deficiencies noted on the unit inspection.
Criteria	<p>Code of Federal Regulations 24, Subpart I, Section 982.158 (d) and 982.405 (b) states that the PHA must inspect the unit leased to a family at least annually to determine if the unit meets Housing Quality Standards (HQS) and the PHA must conduct quality control re-inspections. Also the PHA must prepare a unit inspection report.</p>

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-20 (continued)**

Criteria (continued) Code of Federal Regulations 24, Sections 982.158 (d) and 982.404 establish that for units under contract that fail to meet HQS, the PHA must require the owner to correct any cited life threatening HQS deficiencies within 24 hours after the inspections and all other HQS deficiencies within 30 calendar days or within a specified PHA-approved extensions. If the owner does not correct the cited HQS deficiencies within the specified correction period the PHA must stop the Housing Assistance Payment or must terminate the HAP contract. Also, for family-cause defects, if the family does not correct the cited HQS deficiencies within the specified correction period, the PHA must take prompt and vigorous action to enforce the family obligations.

Cause of Condition Management does not maintain adequate monitoring procedures to assure that annual inspections and quality control re-inspections were properly performed and documented in participants files and to assure that adequate follow up procedures were realized by the management to assure that the exceptions detailed in the inspection report are corrected in the required period as required in the Housing Quality Standards Enforcement.

Effect of Condition The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Section 982.158 (d) and 982.405 (b) and 982.404.

Recommendation We recommend management to improve monitoring procedures to assure that annual inspections and quality control re-inspections are properly documented in the participant files and to assure that the exceptions detailed in the inspection reports are duly corrected by the owner or the participant in the required period.

Questioned Costs None.

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2002

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
01-04	14.228	<u>Municipality did not apply adequately the monitoring system developed to ensure contractors compliance with payment of prevailing wages rates to employees.</u> No corrective action has been taken.
01-05	14.228	<u>The Municipality did not maintain adequate property records.</u> No corrective action has been taken.
01-06	14.228	<u>Procurement and Suspension and Debarment – Contract’s Provisions</u> No corrective action has been taken.
00-III-02	14.228	<u>The Davis-Bacon Act monitoring system procedures should be applied consistently</u> No corrective action has been taken.
00-III-03	14.228	<u>Procurement process should by adequately documented</u> No corrective action has been taken.