

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

MUNICIPIO DE LUQUILLO
AUDITORIA 2005-2006
30 DE JUNIO DE 2006

OFICINA DEL COMISIONADO
DE ASUNTOS MUNICIPALES

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO
BASIC FINANCIAL STATEMENTS
WITH THE ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT
YEAR ENDED JUNE 30, 2006

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

BASIC FINANCIAL STATEMENTS
WITH THE ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT

YEAR ENDED JUNE 30, 2006

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

BASIC FINANCIAL STATEMENTS
WITH THE ADDITIONAL REPORTS AND INFORMATION
REQUIRED BY THE SINGLE AUDIT ACT

YEAR ENDED JUNE 30, 2006

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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 financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Luquillo, Puerto Rico**, as of and for the year ended June 30, 2006, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

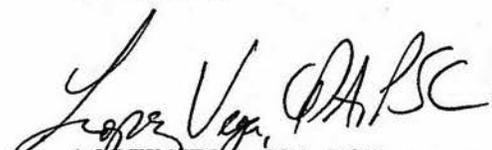
In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Luquillo, Puerto Rico**, as of June 30, 2006, and the respective changes in financial position, thereof 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 28, 2006, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis on pages 3 through 12 and the Budgetary Comparison Schedule-General Fund on page 40 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

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


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
November 28, 2006

Stamp No. 2196002 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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2006

This discussion and analysis of the Municipality of Luquillo (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2006. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2005, second year of implementation of Governmental Accounting Standards Board (GASB) Statement No. 34, "*Basic Financial Statements - and Management's Discussion and Analysis-for State and Local Governments.*" This MD & A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

1. a broader basis in focusing important issues;
2. acknowledgement of an overview of the Municipality's financial activities;
3. provide for an evaluation of its financial condition as of the end of the fiscal year 2005-2006, compared with prior year results;
4. identification of uses of funds in the financing of the Municipality's variety of activities and;
5. assess management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

The financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2006 constitute factual evidence of the Municipality's economic strength by the end of such year. The following comments deserve special mention:

1. At the end of fiscal year 2006, total liabilities amounted to \$11,778,300. Out of said amount, \$9,490,625 corresponded to long-term liabilities of which \$6,826,000 represented the outstanding balance of bonds and notes issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues;
2. Total net assets of the Municipality amounted to \$15,667,978 which represents an increase of 1% compared to prior fiscal year;
3. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$11,425,147, derived from the following sources: \$96,331 charges for services; \$1,983,077 from operating grants and contributions; \$224,723 from capital grants and contributions obtained from other sources, and \$9,121,016 from general revenues available;

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

FINANCIAL HIGHLIGHTS (CONTINUED)

4. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$11,200,836;
5. As reflected in the Statement of Activities, the current fiscal year operations contributed to the increase in the Net Assets Figure by \$224,311;
6. As of the close of the current fiscal, the Municipality's Governmental Funds reported combined ending fund balances of \$5,696,282;
7. At the end of the current fiscal year, the Municipality's General Fund balance amounted to \$2,624,585. It is pertinent to note that it is the municipal administration's contention that the importance of such figure should not be overestimated since it has adopted the policy to use internal generated resources to increase services to Municipality's community rather than let them unused in the accounted records;
8. The actual General Fund budgetary activities resulted in a favorable balance of \$772,615 which is indicative of full compliance with the balanced budget principle applicable to all municipalities of the Commonwealth Government of Puerto Rico as required by the Municipal Autonomous Act enacted in August 1991.
9. In response to the continued increments in the municipal operating revenues, the Municipal Legislature approved a revision to the General Fund Budget for fiscal year 2006 which amounted to \$551,674.

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2006. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

Under the aforementioned approach, assets and liabilities are recognized using the accrual basis of accounting which is similar to the method used by most private enterprises. This means that current year's revenues and expenses are accounted for regardless of when cash is received or paid.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

FINANCIAL STATEMENTS COMPONENTS

The basic financial statements consist of the government wide financial statements, the major funds financial statements and the notes to the financial statements which provide details, disclosure and description of the most important items included in said statements.

The Statement of Net Assets reflects information of the Municipality as a whole on a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year. Such financial level is measured as the difference between total assets and liabilities, with the difference between both items reported as net assets. It is important to note that although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations. The higher the increments achieved in net revenues, the higher the capacity to increase the net assets figure either thru additional borrowings or thru internally generated funds. This in turn will benefit the welfare of the constituents.

The Statement of Activities is focused on both gross and net cost of the various activities of the Municipality. It presents information which shows the changes in the Municipality's net assets at the most recent fiscal year. Based on the use of the accrual basis of accounting, changes are reported as soon as the underlying event occurs, regardless of the timing of the related cash flows. Under said approach, revenues and expenses are reported in the Statement of Activities based on the theory that it will result in cash flows to be realized in future periods.

A brief review of The Statements of Activities of the Municipality at June 30, 2006, shows total expenses incurred to afford the cost of all functions and programs amounted to \$11,200,836. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$2,304,131 was derived from the following sources: \$96,331 charges for services; \$1,983,077 from operating grants and contributions; and \$224,723 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$9,121,016. When such figure is added to the \$2,304,131 previously mentioned, total revenues available for the financing of activities amounted to \$11,425,147. There was an excess of revenues over expenses in the amount of \$224,311 which contributed to the figure of net assets attained at the end of the fiscal year.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

The Fund Financial Statement is another important component of the Municipality's financial statements. A fund is a grouping of related accounts that are used to maintain accountability and controls over economic resources of the Municipality that have been segregated for specific activities. The Municipal fund type of accounting is used to demonstrate compliance with related legal requirements. Information offered thru this Statement is limited to the Municipality most significant funds and is particularly related to the local government only, instead of the government as a whole. Government funds are used to account for essentially the same functions as those reported as governmental activities. The funds are reported using an accounting method known as modified accrual accounting which measures cash and all other financial assets that can be readily converted into cash.

The fund statement approach gives the user a short term view of the Municipality's government operations and the basic services it provides. Since the focus of government funds is narrower than that of the financial statements as a whole, it also helps the user with comparable information presented in the governmental activities report. By doing so, readers of the basic financial statements may understand better the long-term effect of the Municipality's short-term financial decisions.

INFRASTRUCTURE ASSETS

Historically, a significant group of infrastructure assets such as roads, bridges, traffic signals, underground pipes not associated with utilities, have not been recognized nor depreciated in the accounting records of the Municipality. GASB 34 requires that such type of assets be inventoried, valued and reported under the governmental column of the Government-Wide Statement. As explained in the Capital Assets and Debt Administration Section of this MD&A, on July 1, 2002, the Municipality commenced partially the prospective reporting of infrastructure assets. The Municipality expects to retroactively report historical costs of infrastructure assets during the fiscal year beginning on July 1, 2006.

According to the requirements of GASB 34, the government must elect to either (a) depreciate the aforementioned assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery to near perpetuity. If the government develops the asset management system, (the modified approach) which periodically (at least every three years), by category, measures and demonstrate its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. In this particular respect, the Municipality has elected the use of recognizing depreciation under the useful life method and it contemplates to continue this treatment on said basis.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

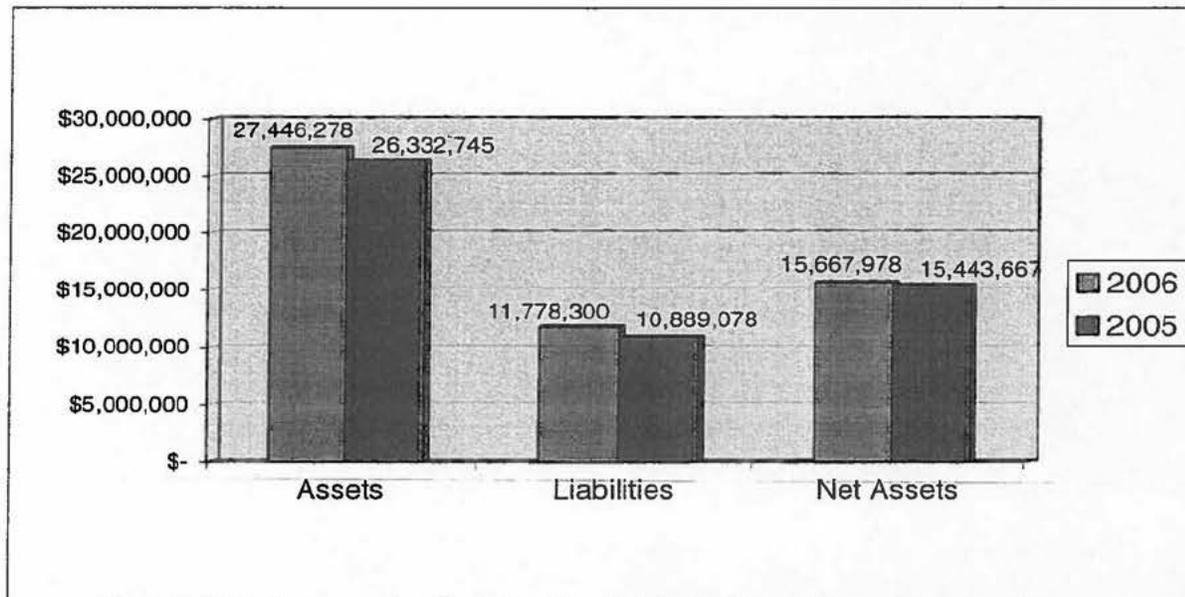
YEAR ENDED JUNE 30, 2006

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Luquillo, primary government assets exceeded total liabilities by \$15,667,978 at the end of 2006, compared to \$15,443,667 at the end of the previous year, as showed in the following condensed Statement of Net Assets of the Primary Government.

Condensed Statement of Net Assets	2006	2005	Change	%
Current and other assets	\$ 7,668,107	\$ 7,538,865	\$ 129,242	2%
Capital assets	19,778,171	18,793,880	984,291	5%
Total assets	27,446,278	26,332,745	1,113,533	4%
Current and other liabilities	2,287,675	2,029,859	257,816	13%
Long-term liabilities	9,490,625	8,859,219	631,406	7%
Total liabilities	11,778,300	10,889,078	889,222	8%
Invested in capital assets, net of related debt	13,898,421	13,541,880	356,541	3%
Restricted	2,916,610	3,909,044	(992,434)	(25%)
Unrestricted deficit	(1,147,053)	(2,007,257)	860,204	(43%)
Total net assets	\$ 15,667,978	\$ 15,443,667	\$ 224,311	1%



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Changes in Net Assets

The Statement of Activities reflects that for fiscal year 2006, the net effect of the revenues derived from several programs plus current operating revenues compared to the total expense, amounted to \$224,311. Approximately 46 percent of the Municipality's total revenues resulted from grants and contributions, including federal aid, while 50 percent came from taxes. The largest expenses were for general government, public works, health and welfare, culture and recreation, and public safety. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

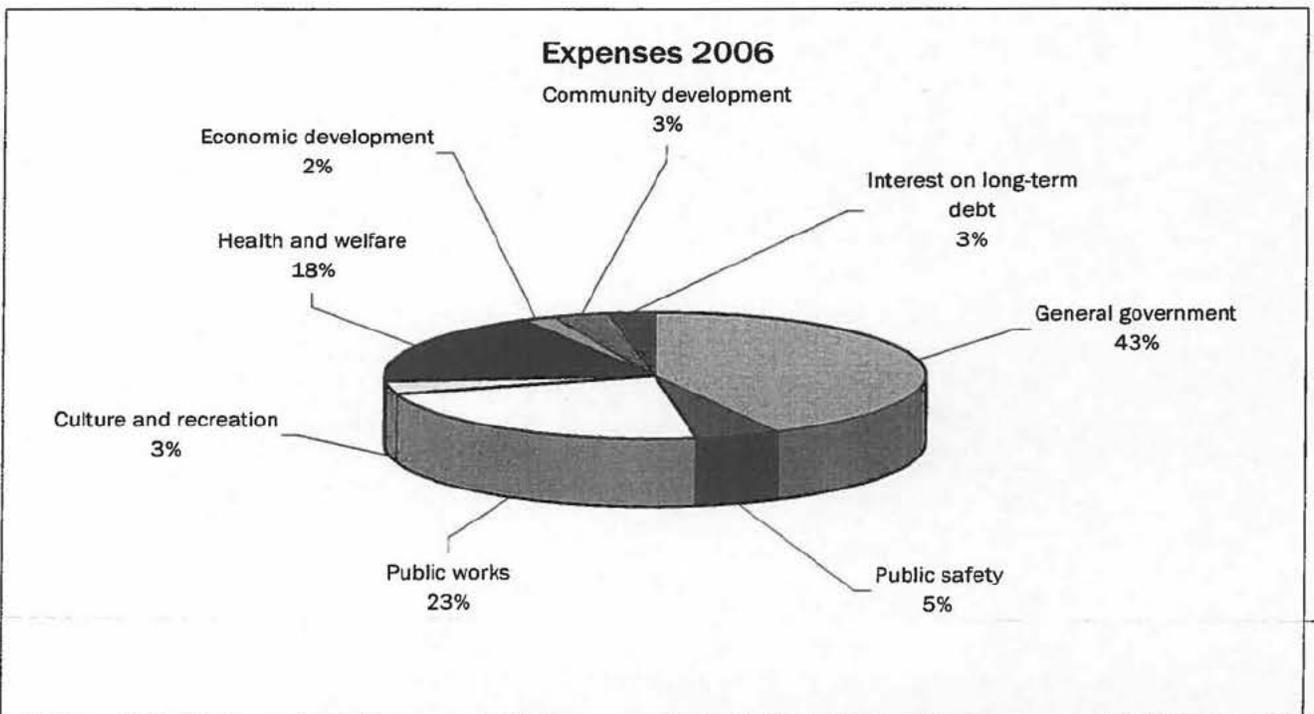
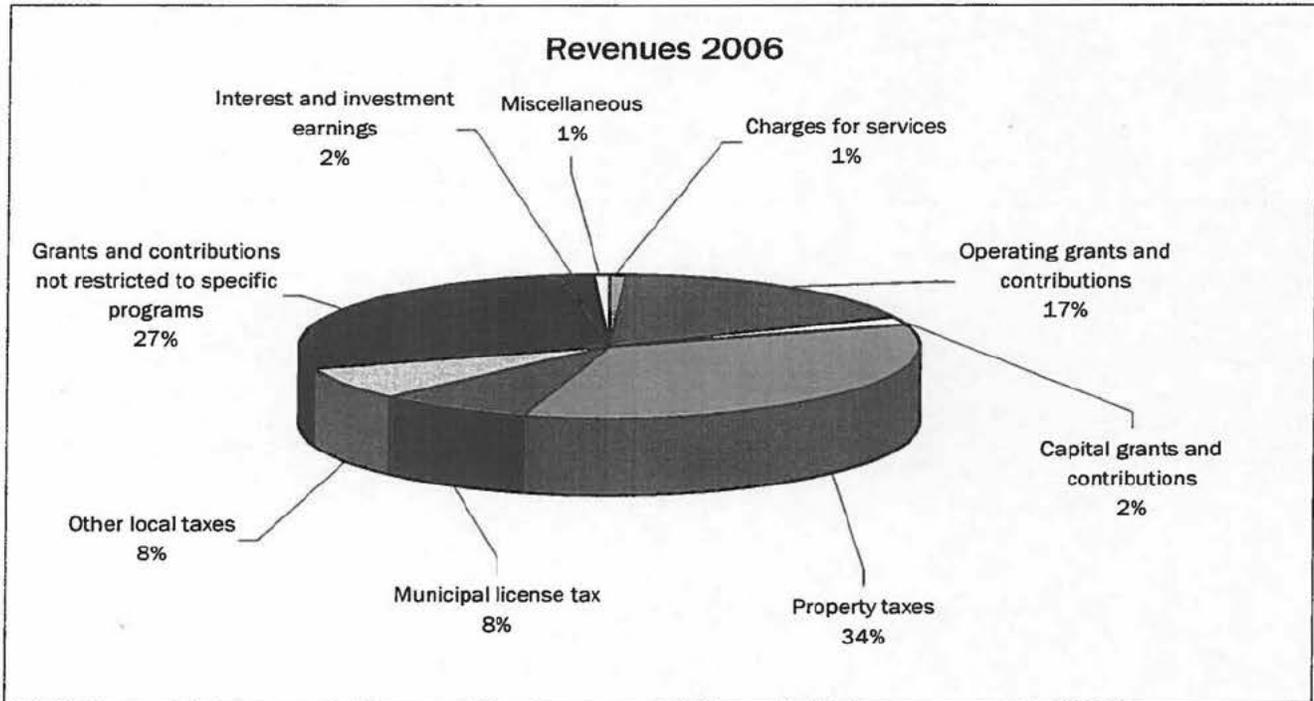
Condensed Statement of Activities	2006	2005	Change	%
Program revenues:				
Charges for services	\$ 96,331	\$ 88,773	\$ 7,558	9%
Operating grants and contributions	1,983,077	2,635,112	(652,035)	(25%)
Capital grants and contributions	224,723	320,381	(95,658)	(30%)
General revenues:				
Property taxes	3,912,762	3,875,754	37,008	1%
Municipal license tax	922,998	893,301	29,697	3%
Other local taxes	857,914	583,202	274,712	47%
Grants and contributions not restricted to specific programs	3,110,566	2,536,469	574,097	23%
Interest and investment earnings	229,903	183,551	46,352	25%
Miscellaneous	86,873	28,448	58,425	205%
Total revenues	11,425,147	11,144,991	280,156	3%
Expenses:				
General government	4,769,529	4,098,810	670,719	16%
Public safety	561,698	336,072	225,626	67%
Public works	2,539,988	2,150,535	389,453	18%
Culture and recreation	386,209	389,459	(3,250)	(1%)
Health and welfare	2,036,672	2,108,142	(71,470)	(3%)
Economic development	227,505	317,224	(89,719)	(28%)
Community development	364,730	131,369	233,361	178%
Education	-	3,034	(3,034)	(100%)
Interest on long-term debt	314,505	315,743	(1,238)	-
Total expenses	11,200,836	9,850,388	1,350,448	14%
Change in net assets	224,311	1,294,603	(1,070,292)	(83%)
Net assets, beginning of year, as restated	15,443,667	14,149,064	1,294,603	9%
Net assets, end of year	\$ 15,667,978	\$ 15,443,667	\$ 224,311	1%

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

As noted earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

Governmental Funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$5,696,282, a decrease of \$(220,593) in comparison with the prior year. There are reservations of fund balance amounting to \$3,476,223. This is the fund balance that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior fiscal year (\$404,526), 2) to pay debt service (\$1,898,896), 3) to pay for capital projects (\$949,131) and 4) for other purposes (\$223,670).

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2006, the general fund has an undesignated fund balance of \$2,220,059.

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the Municipality Council revised the Municipality's budget in order to include increases in revenues that were identified during the course of the fiscal year based on current developments that positively affected the Municipality's finances. Increases in budgeted expenditures were also made since the law mandates a balanced budget.

In response to the increments in the municipal operating revenues, the Municipal Legislature approved a revision to the General Fund Budget for fiscal year 2006 which amounted to \$551,674. Such increments were used to provide further increases in capital assets and for the extension of several municipal services to Luquillo's communities.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2006

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2006, amounts to \$26,936,145, net of accumulated depreciation of \$7,157,974 (including \$641,885 of current year depreciation expense), leaving a net book value of \$19,778,171. This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure, furnishing, computers and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2006, the Municipality has \$1,034,724 of unexpended proceeds from bond and notes issuances that are committed to future construction activities.

Debt Administration

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged.

The applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes such Municipality must have sufficient "payment capacity". Act No. 64 provides that a Municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, will be sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2006

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available but the revenue also is very predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2006-2007.

FINAL COMMENTS

The Municipality is an autonomous governmental entity whose powers and authority vested on its Executive and Legislative Branches are specifically established in the Municipal Autonomous Act approved in August 1991. By virtue of such powers, it provides a wide range of services to its constituents which includes, among others, public works, education, public safety, public housing, health, community development, recreation, waste disposal, welfare and others. The Municipality's principal sources of revenues are derived from property taxes, municipal license taxes, subsidies from the Commonwealth of Puerto Rico's General Fund and contributions from the Traditional and Electronic Lottery sponsored by said Government.

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. Such has been the case of the financial operation corresponding to fiscal year 2006. It further contemplates to improve its current figure of net assets, which has been identified as one of the main short and long-term objectives of the Municipality.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at P.O. Box 1012, Luquillo, Puerto Rico 00773-1012, or call (787) 889-2068.

Commonwealth of Puerto Rico
Municipality of Luquillo
Statement of Net Assets
June 30, 2006

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 3,944,500
Cash with fiscal agent	3,248,218
Accounts receivable:	
Intergovernmental	453,915
Interest	21,474
Capital assets	
Land, improvements, and construction in progress	7,892,714
Other capital assets, net of depreciation	11,885,457
Total capital assets	19,778,171
 Total assets	 27,446,278
 Liabilities	
Accounts payable and accrued liabilities	1,071,975
Due to other governmental entities	32,398
Interest payable	155,087
Deferred revenues:	
Municipal license tax	674,695
Federal grant revenues	353,520
Noncurrent liabilities:	
Due within one year	565,519
Due in more than one year	8,925,106
Total liabilities	11,778,300
 Net Assets	
Invested in capital assets, net of related debt	13,898,421
Restricted for:	
Capital projects	949,131
Debt service	1,743,809
Other purposes	223,670
Unrestricted (deficit)	(1,147,053)
 Total net assets	 \$ 15,667,978

Commonwealth of Puerto Rico
Municipality of Luquillo
Statement of Activities
For the Year Ended June 30, 2006

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
General government	\$ 4,769,529	\$ -	\$ 118,604	\$ -	\$ (4,650,925)
Public safety	561,698	10,145	164,206		(387,347)
Public works	2,539,988	16,718	198,228	224,723	(2,100,319)
Health and welfare	2,036,672	25,448	794,442		(1,216,782)
Culture and recreation	386,209	29,785	8,295		(348,129)
Economic development	227,505	14,235	220,575		7,305
Community development	364,730		478,727		113,997
Interest on long-term debt	314,505				(314,505)
Total governmental activities	\$ 11,200,836	\$ 96,331	\$ 1,983,077	\$ 224,723	(8,896,705)
General revenues:					
Property taxes					3,912,762
Municipal license tax					922,998
Other local taxes					857,914
Grants and contributions not restricted to specific programs					3,110,566
Interest and investment earnings					229,903
Miscellaneous					86,873
Total general revenues					9,121,016
Change in net assets					224,311
Net assets - beginning, as restated					15,443,667
Net assets - ending					\$ 15,667,978

Commonwealth of Puerto Rico
Municipality of Luquillo
Balance Sheet
Governmental Funds
June 30, 2006

	General Fund	Special Revenue Fund - Local & State Grants	Special Revenue Fund Federal Grants	Capital Projects Fund - Local & State Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Assets							
Cash and cash equivalents	\$ 2,967,181	\$ 514,353	\$ 344,763	\$ -	\$ -	\$ 118,203	\$ 3,944,500
Cash with fiscal agent		62,013	129,303	1,251,533	1,805,369		3,248,218
Accounts receivable:							
Intergovernmental			124,428	224,723	104,764		453,915
Interest	15,572				5,902		21,474
Due from other funds	743,045	53,820					796,865
Total assets	\$ 3,725,798	\$ 630,186	\$ 598,494	\$ 1,476,256	\$ 1,916,035	\$ 118,203	\$ 8,464,972
Liabilities and Fund Balances							
Liabilities :							
Accounts payable and accrued liabilities	\$ 394,120	\$ 3,720	\$ 94,109	\$ 419,263	\$ -	\$ -	\$ 911,212
Due to other governmental entities	32,398						32,398
Due to other funds		402,796	249,886	107,862	17,139	19,182	796,865
Deferred revenues:							
Municipal license tax	674,695						674,695
Federal grant revenues			254,499			99,021	353,520
Total liabilities	1,101,213	406,516	598,494	527,125	17,139	118,203	2,768,690
Fund balances:							
Reserved for:							
Encumbrances	404,526						404,526
Capital projects				949,131			949,131
Other purposes		223,670	-				223,670
Debt service					1,898,896		1,898,896
Unreserved:							
Undesigned	2,220,059						2,220,059
Total fund balances	2,624,585	223,670	-	949,131	1,898,896	-	5,696,282
Total liabilities and fund balances	\$ 3,725,798	\$ 630,186	\$ 598,494	\$ 1,476,256	\$ 1,916,035	\$ 118,203	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	19,778,171
Long-term liabilities, including non current accounts payable and accrued interests payable, are not due and payable in the current period, and therefore, are not reported in the funds	(9,806,475)
Net assets of governmental activities	\$ 15,667,978

Commonwealth of Puerto Rico
Municipality of Luquillo
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2006

	General Fund	Special Revenue Fund - Local & State Grants	Special Revenue Fund Federal Grants	Capital Projects Fund -Local & State Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Revenues							
Property taxes	\$ 3,006,791	\$ -	\$ -	\$ -	\$ 905,972	\$ -	\$ 3,912,763
Municipal license taxes	922,998						922,998
Licenses, permits and other local taxes	857,914						857,914
Charges for services	50,780						50,780
Intergovernmental	3,229,169	331,628	10,030	224,723		28,026	3,823,576
Rent of property	22,150						22,150
Fines and forfeitures	10,145						10,145
Interest	229,903						229,903
Federal grants			1,073,317			412,885	1,486,202
Miscellaneous	86,492	8,968	13,256				108,716
Total revenues	8,416,342	340,596	1,096,603	224,723	905,972	440,911	11,425,147
Expenditures							
Current:							
General government	4,272,401			290,558			4,562,959
Public safety	242,898	195,227	165,206				603,331
Public works	1,740,007	731,993	91,107	365,403			2,928,510
Health and welfare	1,200,386	2,793	362,563			440,911	2,006,653
Culture and recreation	205,492	15,299		708,431			929,222
Economic development	15,573	211,514					227,087
Community development			478,727				478,727
Principal					291,000		291,000
Interest					303,251		303,251
Total expenditures	7,676,757	1,156,826	1,097,603	1,364,392	594,251	440,911	12,330,740
Excess (deficiency) of revenues over (under) expenditures	739,585	(816,230)	(1,000)	(1,139,669)	311,721	-	(905,593)
Other financing sources (uses)							
Transfers in	21,002			26,781			47,783
Transfers out		(26,781)			(21,002)		(47,783)
Long-term debt issued		685,000					685,000
Total other financing sources (uses)	21,002	658,219	-	26,781	(21,002)	-	685,000
Net change in fund balances	760,587	(158,011)	(1,000)	(1,112,888)	290,719	-	(220,593)
Fund balances, beginning	1,863,998	381,681	1,000	2,062,019	1,808,177		5,916,875
Fund balances, ending	\$ 2,624,585	\$ 223,670	\$ -	\$ 949,131	\$ 1,898,896	\$ -	\$ 5,696,282

The notes to the financial statements are an integral part of this statement.

Commonwealth of Puerto Rico
Municipality of Luquillo
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2006

Net Change in Fund Balances - Total Governmental Funds \$ (220,593)

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period. 1,630,946

Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds. (641,885)

Disposal of capital assets require removal of cost of the capital assets from the capital asset account on the Government-Wide Statement of Net Assets, resulting in a loss on disposal of capital assets on the Government-Wide Statement of Activities and Changes in Net Assets. (279)

Governmental Funds report capital assets sold as revenues. However, in the Government-Wide Statement of Activities and Changes in Net Assets, capital assets sold require removal of cost of the capital assets from the capital asset account on the Government-Wide Statement of Net Assets. (2,242)

Interest Payable on long-term debt was reported in the Government-Wide Statement of Activities and Changes in Net Assets, but it did not require the use of current financial resources. Therefore, Interest Payable was not reported as expenditures in Governmental Funds. The following amount represents the change in accrued interest from prior year. (11,254)

Accounts Payable reported in the Government-Wide Statement of Activities and Changes in Net Assets but not reported as in the Governmental Funds because they do not require the use of current financial resources. The following amount represents the change in this accounts payable from prior year. 103,271

Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long-term liabilities in the Government-Wide Statement of Net Assets. This is the amount by which the debt proceeds exceed debt service principal payments. (394,000)

Repayment of long-term property tax advance debt is an expenditure in Governmental Funds, but the repayment reduces long-term property tax advance debt in the Government-Wide Statement of Net Assets. This is the change in the property tax advance debt in the current period. (40,639)

Long-term compensated absences are reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represented the change in long-term compensated absences from prior year. (104,114)

Repayment of long term Puerto Rico Land Authority debt is an expenditure in Governmental Funds, but the repayment reduces long-term debt in the Government-Wide Statement of Net Assets. This is the long term Puerto Rico Land Authority debt recorded in the current period. (133,350)

Repayment of long term Land Information Management System (LIMS) is an expenditure in Governmental Funds, but the repayment reduces long term LIMS in the Government-Wide Statement of Net Assets. This is the amount paid in the current period. 38,450

Change in Net Assets of Governmental Activities \$ 224,311

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2006

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Luquillo** (the Municipality) was founded on the year 1797. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a twelve member Municipal Legislature who are elected for a four-year term.

The Municipality provides a full range of services for its citizens. These services include public safety, public works, culture and recreation, health and welfare, community development, education, and other miscellaneous services.

The accounting policies and financial reporting practices of the Municipality conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units.

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's and Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. The Statement was adopted as of July 1, 2002. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

As part of this Statement, there is a new reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). This requirement permits an optional four-year delay for implementation to fiscal year ended on June 30, 2007. The Municipality has elected to delay the capitalization of infrastructure.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

The following is a summary of the significant accounting policies of the Municipality:

A. Component Units

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, The Financial Reporting Entity, of the GASB, as amended by GASB Statement No. 39. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary government appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

B. Government-wide and fund financial statements

Financial information of the Municipality is presented in this report as follow:

1. Management's discussion and analysis introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
2. The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all the activities of the Municipality and its component units, if any. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, if any, which rely to a significant extent on fees and charges for support. Interfund activity has been removed from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenue. Direct expenses are those that are charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The Municipality reports the following major governmental funds:

General Fund – is the accounting entity in which all governmental activity, except that which is required to be accounted for in another fund, is accounted for. Its revenues consist mainly of taxes, licenses and permits, intergovernmental revenue, charges for services and other.

Special Revenue Fund – State and Local Grants – is the accounting entity in which revenues derived from local funds, state or other restricted revenue source is accounted for the uses and limitations specified by Municipality ordinances or state statutes.

Special Revenue Fund – Federal Grants – is the accounting entity in which revenues derived from federal grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Projects Fund – Local and State Grants – is the accounting entity in which revenues derived from local funds and state grants or other restricted revenue sources related to capital projects, is accounted for. The uses and limitations of each capital project fund are specified by Municipality ordinances and state statutes.

Debt Service Fund – is the accounting entity used to account for the resources accumulated and payments made for principal and interest on long-term general obligation bonds of governmental funds.

4. The notes to the financial statements provide information that is essential to a user's understanding of the basic financial statements.
5. Required supplementary information such as the budgetary comparison schedule-general fund and other types of data required by GASB.
6. Notes to the budgetary comparison schedule-general fund.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

C. Financial reporting presentation

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Fund types are as follows:

General Fund – General Fund is the general operating fund of the Municipality. It is used to account for all governmental activity, except those required to be accounted for in another fund.

Special Revenue Fund – Local and State Grants – Special Revenue Funds are used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund – Section 8 – Special Revenue Funds are used to account for revenues derived from Section 8 Housing Choice Voucher Program. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund – Federal Grants – Special Revenue Funds are used to account for revenues derived from federal grants. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Projects Fund – Local and State Grants – Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

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

D. Measurement focus, basis of accounting and financial presentation

Except for budgetary purposes, the basis of accounting used by the Municipality conform to accounting principles generally accepted in the United States of America (“GAAP”) as applicable to governmental units. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The Municipality has elected not to apply all Statements and Interpretations issued by the Financial Accounting Standard Board after November 30, 1989, in accordance with GASB Statement No. 20.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures when payment is due. General capital asset acquisitions are reported as expenditure in governmental funds. Proceeds from issuance of general long-term debt reported as other financing sources.

Property taxes, franchise taxes, licenses, rent, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

Private-sector standards of accounting and financial reporting issue prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants, and contributions, and 3) capital grants and contributions, including special assessments, if any. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

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

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

E. Assets, liabilities and net assets

- 1. Cash, cash equivalents, and cash with fiscal agent** – The Municipality's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

Cash with fiscal agent in the debt services fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law.

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

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

Receivables are stated net of estimated allowance for uncollectible accounts, which are determined, based upon past collections experience and current economic conditions. Intergovernmental receivables in the General Fund represent mostly charge for services rendered to other governmental entities. Intergovernmental receivable in the special revenue or capital project funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded or state funded programs.

- 3. Inventories** – Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

4. **Capital assets** – Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets of the Municipality are depreciated using the straight-line method over the following estimated useful lives:

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Buildings and site improvements	40 years	\$1
Infrastructure	40 years	\$1
Works of art	10 years	\$1
Vehicles	5 years	\$1
Furniture and fixtures	5 years	\$25
Machinery and equipment	3 to 5 years	\$25

5. **Long-term obligations** – The liabilities reported in the government-wide financial statements included general and special obligation bonds and notes, and other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

6. **Compensated absences** – Employees accumulate vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. All vacation pay is accrued when incurred in the government-wide financial statements.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

7. **Claims and judgments** – The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.
8. **Reservation of fund balance** – Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The municipality has the following reservations of fund balance:
- a. **Capital Projects** – Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
 - b. **Encumbrances** – Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
 - c. **Other Purposes** – Represents net assets available for specific use and/or legally segregated for other specific future use.
 - d. **Debt Service Fund** – Represents net assets available to finance future debt service payments.
9. **Interfund and intra-entity transactions** – The Municipality has the following types of transactions among funds:
- a. **Operating Transfers** – Legally required transfers that are reported when incurred as “Operating transfer-in” by the recipient fund and as “Operating transfers-out” by the disbursing fund.
 - b. **Intra-Entity Transactions** – Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
10. **Risk financing** – The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center (CRIM) for the year ended June 30, 2006 amounted to approximately \$160,951. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$190,396 for workers compensation insurance covering all municipal employees.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

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

11. Reconciliation of Government-wide and Fund Financial Statements

The governmental fund balance sheet includes reconciliation between fund balance-total governmental funds and net assets-governmental activities as reported in the government-wide statement of net assets. The two elements of that reconciliation explains that "long term liabilities, including compensated absences, bonds and notes payable, are not due and payable in the current period and therefore are not reported in the funds.", and that "capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds." The details of this reconciliation are as follows:

		<u>Total Net Assets - Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 19,778,171	
Deduct:		
Bonds Payable	(4,525,000)	
Notes Payable	(1,231,000)	
Land Authority debt	<u>(123,750)</u>	\$ 13,898,421
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		949,131
<u>Net assets restricted for debt service</u>		
Debt service fund - fund balances	\$ 1,898,896	
Deduct:		
Interest payable	<u>(155,087)</u>	1,743,809
<u>Net assets restricted for other purposes</u>		
Special Revenue Fund - Local and State Grants - fund balance restricted for other purposes		223,670
<u>Net assets unrestricted (deficit)</u>		
General fund - total fund balance:	\$ 2,624,585	
Deduct:		
Accounts Payable	(160,763)	
Bond and Notes Payable	(1,070,000)	
Compensated absences debt	(970,136)	
Advance property taxes debt	(1,304,199)	
LIMS repayment plan	(256,940)	
Land Authority debt	<u>(9,600)</u>	<u>(1,147,053)</u>
Total net assets - governmental activities		<u>\$ 15,667,978</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

2. DEPOSITS

Under Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The Municipality's bank balances in commercial banks of approximately \$2,967,181 in the General Fund, the \$514,353 in the Special Revenue Fund – Local and State Grants and the \$344,763 in the Special Revenue Fund – Federal Grants were fully collateralized at June 30, 2006. In the Other Governmental Funds there were deposits with commercial banks of approximately \$118,203 that were fully collateralized.

The deposits at GDB of approximately \$62,013 in the Special Revenue Fund – Local and State Grants, the \$129,303 in the Special Revenue Fund – Federal Grants, the \$1,251,533 in the Capital Projects Fund – Local and State Grants that are restricted principally for capital projects, and the \$1,805,369 in the Debt Service Fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

A. *Municipal License Tax* – The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Act of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2006, the tax rates were as follows:

1. Financial business – 1.50% of gross revenues.
2. Other organizations – 0.50% of gross revenues.

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2006, net of allowance for uncollectibles.

Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

3. RECEIVABLES (CONTINUED)

Intergovernmental Receivables – Intergovernmental receivables in the Special Revenue Fund – Federal Grants represent expenditures incurred not yet reimbursed by the federal government or the pass-through grantor. Following is a detail of the intergovernmental receivables:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grants – State's Program	\$ 74,604
Pre-disaster Mitigation Competitive Grant	37,305
Child Care and Development Block Grant	9,824
Community Service Block Grant	<u>2,695</u>
Total	<u>\$ 124,428</u>

Intergovernmental receivables in the Capital Project Fund – Local and State Grants represent expenditures incurred not yet reimbursed by the other governmental entities. Following is a detail of the intergovernmental receivables:

<u>Governmental Entity</u>	<u>Amount</u>
Commonwealth of Puerto Rico – Legislature (Law 43)	<u>\$ 224,723</u>
Total	<u>\$ 224,723</u>

Intergovernmental receivable in the Debt Service Fund represents the amounts due from the CRIM resulting from the excess of current year property tax collections over current year advances. Following is a detail of the intergovernmental receivable:

<u>Governmental Entity</u>	<u>Amount</u>
Municipal Revenue Collection Center (CRIM)	<u>\$ 104,764</u>
Total	<u>\$ 104,764</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2006 are summarized as follows:

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund – Local and State Grants	Payrolls, accruals, and other expenditures not reimbursed	\$ 402,796
General Fund	Special Revenue Fund – Federal Grants	Payrolls, accruals, and other expenditures not reimbursed	249,886
General Fund	Capital Project Fund – Local and State Grants	Payrolls, accruals, and other expenditures not reimbursed	54,042
General Fund	Debt Service Fund	Interest not transferred	17,139
General Fund	Other Governmental Funds	Payrolls, accruals, and other expenditures not reimbursed	19,182
Special Revenue Fund – Local and State Grants	Capital Project Fund – Local and State Grants	Cash pool in the same bank account	<u>53,820</u>
Total			<u>\$ 796,865</u>

b. Transfer in/out to other fund

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
Debt Service Fund	General Fund	Residual equity transfer	\$ 21,002
Special Revenue Fund – Local and State Grants	Capital Project Fund	Reimbursable expenditures	<u>26,781</u>
Total			<u>\$ 47,783</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

5. CAPITAL ASSETS

Capital assets; those with an estimated useful live of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2006, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<u>Governmental Activities:</u>	<u>Balance</u> <u>July 1, 2005</u> <u>as restated</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance</u> <u>June 30, 2006</u>
Capital asset, not being depreciated:				
Land	\$ 4,315,074	\$ -	\$ (2,242)	\$ 4,312,832
Construction in progress	<u>2,670,072</u>	<u>1,069,832</u>	<u>(160,022)</u>	<u>3,579,882</u>
Total capital assets not being depreciated	<u>6,985,146</u>	<u>1,069,832</u>	<u>(162,264)</u>	<u>7,892,714</u>
Capital assets, being depreciated:				
Buildings	11,355,667			11,355,667
Buildings improvements	1,402,596	2,160		1,404,756
Infrastructure	29,497	3,645		33,142
Infrastructure improvements	1,061,574	530,361		1,591,935
Equipment	1,705,061	144,787	(8,580)	1,841,268
Furnishing	517,836	8,951	(1,754)	525,033
Work of art	400			400
Computers	220,378	13,062	(3,968)	229,472
Vehicles	<u>2,129,961</u>	<u>18,170</u>	<u>(86,373)</u>	<u>2,061,758</u>
Total capital assets being depreciated	<u>18,422,970</u>	<u>721,136</u>	<u>(100,675)</u>	<u>19,043,431</u>
Less accumulated depreciation for:				
Buildings	(2,525,290)	(283,891)		(2,809,181)
Buildings improvements	(53,472)	(35,083)		(88,555)
Infrastructure	(1,445)	(821)		(2,266)
Infrastructure improvements	(63,578)	(83,564)		(147,142)
Equipment	(1,464,811)	(94,950)	8,300	(1,551,461)
Furnishing	(470,831)	(26,656)	1,754	(495,733)
Works of art	(123)	(40)		(163)
Computers	(163,940)	(30,418)	3,968	(190,390)
Vehicles	<u>(1,872,995)</u>	<u>(86,462)</u>	<u>86,374</u>	<u>(1,873,083)</u>
Total accumulated depreciation	<u>(6,616,485)</u>	<u>(641,885)</u>	<u>100,396</u>	<u>(7,157,974)</u>
Total capital assets being depreciated, net	<u>11,806,485</u>	<u>79,251</u>	<u>(279)</u>	<u>11,885,457</u>
Governmental activities capital assets, net	<u>\$ 18,791,631</u>	<u>\$ 1,149,083</u>	<u>\$ (162,543)</u>	<u>\$ 19,778,171</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

5. CAPITAL ASSETS (CONTINUED)

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

Governmental activities:	<u>Amount</u>
General government	\$ 285,501
Public works	120,086
Culture and recreation	85,379
Community development	94,340
Health and welfare	32,611
Public safety	23,550
Economic development	<u>418</u>
Total depreciation expense-governmental activities	<u>\$ 641,885</u>

6. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the Municipal Revenue Collection Center (CRIM), a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomous Law of August 1991. Real property tax is assessed by the CRIM on each piece of real estate and on each building.

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the preliminary liquidation noting that the advances exceeded collections by \$49,660. This excess will not be funded with available expendable financial resources at June 30, 2006. Based on this, such amount was presented in the government-wide financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

6. PROPERTY TAXES (CONTINUED)

On December 31, 1992, the Municipality entered into an agreement with the Commonwealth of Puerto Rico – Treasury Department, for the repayment of excess property tax advances. As of June 30, 2006, the related unpaid property taxes advances included in the Statement of Net Assets amounted to \$3,799.

On January 26, 2000, Public Law 42 was enacted which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000. The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law 238, enacted on August 15, 1999. On October 11, 2001, Public Law 146 was enacted to amend Public Law 42, to extend the loan amortization period up to 30 years. Also, on October 11, 2003, Public Law 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law 42 enacted on January 26, 2000.

On June 26, 1997, Public Law Num. 21 was enacted authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable or equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities thru a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law.

The government-wide Statement of Net Assets includes an outstanding balance of \$700,940 and \$549,800 related to Law 146 and the Law 42, respectively.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

6. PROPERTY TAXES (CONTINUED)

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 Puerto Rico Treasury Department assumes payment of the basic tax to the Municipalities, except for property assessed at less than \$3,500 for which no payment is made. As part of the Municipal Autonomous Law of 1991, the exempt amount to be paid by the Puerto Rico Treasury department to the Municipalities was frozen as of January 1, 1992. In addition, the law grants a tax exemption from the payment of personal property taxes of up to \$50,000 of the assessed value to retailers having annual net sales of less than \$150,000.

The annual tax rate is 8.83% for real property and 6.83% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 2.00% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

7. DUE TO OTHER GOVERNMENTAL ENTITIES

The amounts due to other governmental entities in the general fund include the following:

<u>Governmental Entity</u>	<u>Amount</u>
Department of Labor - Unemployment	\$ 29,063
Puerto Rico Aqueduct and Sewer Authority ("AAA")	1,769
Department of Treasury - Income Tax	1,141
General Services Administration	<u>425</u>
Total	<u>\$ 32,398</u>

8. DEFERRED REVENUES

- A. Municipal License Tax** - The deferred revenues of approximately \$674,695 in the General Fund relates to municipal license tax collected in fiscal year 2005-06 that will be earned in fiscal year 2006-07.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

8. DEFERRED REVENUES (CONTINUED)

B. Federal Government – The deferred revenues presented in the Special Revenue Fund – Federal Grants represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Public Assistance Grant	\$ 129,303
Child Care and Development Block Grant	50,362
Special Program, For Aging, Title III	29,756
Edward Byrne Memorial Justice Assistance Grant Program	15,770
Emergency Management Performance Grant	12,322
State and Community Highway Safety Program	10,170
Citizen Corps	4,126
Title V – Delinquency Prevention Program	1,140
Nutrition Program for the Elderly	832
Housing Preservation Grant	<u>718</u>
Total	\$ <u>254,499</u>

The deferred revenues presented in the Other Governmental Funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Section 8 Housing Choice Voucher Program	<u>\$ 99,021</u>
Total	\$ <u>99,021</u>

9. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2006, was as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds Payable	\$ 5,815,000	\$ -	\$ (220,000)	\$ 5,595,000	\$ 235,000
Notes Payable	617,000	685,000	(71,000)	1,231,000	182,000
Property Taxes Advances	1,110,232	202,988	(9,021)	1,304,199	9,528
Land Authority		142,353	(9,003)	133,350	49,750
Compensated Absences	866,022	181,478	(77,364)	970,136	48,469
Municipal Revenue Collection Center – LIMS Repayment Plan	<u>-</u>	<u>295,390</u>	<u>(38,450)</u>	<u>256,940</u>	<u>40,772</u>
Total	\$ <u>8,408,254</u>	\$ <u>1,507,209</u>	\$ <u>(424,838)</u>	\$ <u>9,490,625</u>	\$ <u>565,519</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

9. LONG-TERM LIABILITIES (CONTINUED)

1. **Legal debt margin** – The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds and notes payable, is paid with unrestricted funds.

2. **Bonds payable** – The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. Bonds payable outstanding at June 30, 2006 are as follows:

<u>Type of bonds</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest Rates</u>	<u>Balance at June 30, 2006</u>
1993 Series	7-1-12	\$ 2,015,000	5.00% to 8.00%	\$ 1,070,000
2000 Series	7-1-14	460,000	2.70% to 7.81%	335,000
2003 Series	7-1-27	4,430,000	5.00% to 5.31%	<u>4,190,000</u>
Total general obligation bonds				<u>\$ 5,595,000</u>

These bonds are payable from the ad valorem property tax of 2.00% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

Annual debt service requirements to maturity for bonds payable are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 235,000	\$ 276,935
2008	255,000	279,430
2009	275,000	263,310
2010	295,000	245,776
2011	315,000	226,709
2012-2016	1,255,000	866,670
2017-2021	970,000	627,892
2022-2026	1,330,000	348,878
2027-2031	<u>665,000</u>	<u>34,010</u>
Total	<u>\$ 5,595,000</u>	<u>\$ 3,169,610</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

9. LONG-TERM LIABILITIES (CONTINUED)

3. **Notes Payable** – The proceeds of the issuance of notes payables were used principally to pay debt incurred in prior years and to cover the expenditures of a special event. During the current year, the Municipality issued notes for approximately \$685,000. Notes payable outstanding at June 30, 2006 are as follows:

<u>Type of notes</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest rates</u>	<u>Balance at June 30, 2006</u>
2003 Series	1-1-10	\$ 521,000	4.75%	\$ 318,000
2004 Series	1-1-13	228,000	4.25%	228,000
2006 Series	7-1-12	685,000	4.23% to 5.33%	<u>685,000</u>
Total notes payable				<u>\$ 1,231,000</u>

The notes are payable from the ad valorem property tax of 2.00% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

Annual debt service requirements to maturity for notes payable are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 182,000	\$ 54,750
2008	193,000	48,083
2009	202,000	36,619
2010	212,000	27,466
2011	139,000	17,625
2012-2016	<u>303,000</u>	<u>15,688</u>
Total	<u>\$ 1,231,000</u>	<u>\$ 200,231</u>

4. **Property Taxes Advances Debt** – These amounts represent the balance owed to the Treasury Department and to the Municipal Revenue Collection Center (CRIM) at June 30, 2006, as described in Note 6.
5. **Compensated absences** – The government-wide statement of net assets includes approximately \$493,732 of accrued sick leave benefits, and approximately \$476,404 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.
6. **Land Authority** – This amount represents a payment agreement with the Land Authority for the acquisition of a parcel of land.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

9. LONG-TERM LIABILITIES (CONTINUED)

7. Municipal Revenue Collection Center - LIMS Repayment Plan - During the fiscal year 2001-2002, the Municipality authorized the CRIM to retain the corresponding portion for the financing project of Land Information Management System - LIMS, contracted by the CRIM. A total of \$413,522 is to be retained in a ten years period at an interest rate of 5.95%, until November 28, 2011. At June 30, 2006 the outstanding debt balance is \$256,940. This amount will be presented in the government wide Statement of Net Assets.

10. PENSION PLAN

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

Members who have attained 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have completed ten years of creditable service are entitled to an annual benefit payable monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation, as defined, multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined; otherwise they will receive 75 percent of the average compensation, as defined. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

10. PENSION PLAN (CONTINUED)

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$ 550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total employee and employer contributions during the year ended June 30, 2006 amounted to approximately \$257,659 and \$288,795, respectively.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employee's participation in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 1, 2000, will only be allowed to become members of System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

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

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2006, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940.

11. RISK MANAGEMENT

The Finance Department is responsible of assuring that the Municipality's property is properly insured. Annually, the Finance Department Division compiles the information of all property owned and its respective market value. After evaluating this information, the Finance Department Division submits the data regarding the Municipality's properties to the Public Insurance Department at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

12. CONTINGENCIES

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities.

It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

The Municipality participates in a number of federal financial assistance programs funded by the Federal Government. Expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantor. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the Municipality management expects such amounts, if any, will not be material.

13. SUBSEQUENT EVENTS

A) Sales and Use Tax

On October 4, 2006, the Municipal Legislature, by Ordinance Number 06-2006-2007, authorized the Mayor to impose a sales tax of 1.5%. The dispositions of this Ordinance began on November 15, 2006. The net product of this sales tax will contribute to increase the Municipality's revenues to liquidate its current obligations and to improve the services provided to the citizens.

B) Bond Issuance

On November 1, 2006, the Municipal Legislature authorized the Mayor to accept and apply the funds derived from the donation provided to the Municipality by the Commonwealth of Puerto Rico of the 2006, Series A, Public Improvement Bonds issuance of \$675,000,000. The Municipality of Luquillo will receive a donation of approximately \$1,825,000 during the fiscal year 2006-2007. Those funds will be use to finance several construction and improvements projects.

14. BEGINNING FUND BALANCES AND GOVERNMENTAL ACTIVITIES NET ASSETS RESTATEMENT:

The beginning Governmental Activities Net Assets has been restated by approximately \$(450,965) to properly present the previously reported net assets at June 30, 2005. The restatement is mainly due to the recognition of the Municipal Revenue Collection Center - LIMS Repayment Plan by \$(295,390) and the adjustment of the Property Tax debt balance of Law 42 by \$(153,328).

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

**BUDGETARY COMPARISON SCHEDULE – GENERAL FUND
(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)**

YEAR ENDED JUNE 30, 2006

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 2,678,747	\$ 2,678,748	\$ 3,050,444	\$ 371,696
Municipal license tax	729,439	965,496	944,231	(21,265)
Licenses, permits and other local taxes	323,953	826,824	870,889	44,065
Charges for service	34,780	38,336	50,780	12,444
Intergovernmental	3,203,670	3,226,524	3,229,169	2,645
Rent of property	30,500	20,590	22,150	1,560
Fines and forfeitures	8,000	6,275	10,145	3,870
Interest	131,350	106,599	229,903	123,304
Miscellaneous	<u>250,000</u>	<u>72,721</u>	<u>86,492</u>	<u>13,771</u>
Total revenues	<u>7,390,439</u>	<u>7,942,113</u>	<u>8,494,203</u>	<u>552,090</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
General government	4,031,071	4,408,618	4,290,668	117,950
Public safety	268,275	241,507	241,092	415
Public works	1,555,469	1,763,427	1,750,093	13,334
Health and welfare	1,254,086	1,283,518	1,209,151	74,367
Culture and recreation	228,542	226,817	215,412	11,405
Economic development	17,001	18,226	15,172	3,054
Operating transfer to other fund	<u>35,995</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total expenditures, encumbrances and other financing uses	<u>7,390,439</u>	<u>7,942,113</u>	<u>7,721,588</u>	<u>220,525</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 772,615</u>	<u>\$ 772,615</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule			\$ 8,494,203	
Differences-budget to GAAP:				
GAAP adjustment to revenues				(77,861)
Non-Budgeted transfer in				<u>21,002</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances			<u>\$ 8,437,344</u>	
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule			\$ 7,721,588	
Differences-budget to GAAP:				
GAAP adjustment to expenditures				10,640
Prior year encumbrances recorded as current year expenditures for GAAP basis				224,643
Current year encumbrances recorded as expenditures for budgetary purposes				<u>(280,114)</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances			<u>\$ 7,676,757</u>	

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

NOTES TO BUDGETARY COMPARISON SCHEDULE – GENERAL FUND

YEAR ENDED JUNE 30, 2006

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

a. Budgetary Control

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with GAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the general fund.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.

The unencumbered balance of any appropriation at the end of the fiscal year will lapse at the end of such fiscal year. Other appropriations, mainly capital project appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2006 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2006.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2006

<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>
U.S. DEPARTMENT OF AGRICULTURE:			
Direct Program: Community Facilities Loans and Grants	10.766		\$ 1,000
Total U.S. Department of Agriculture			<u>1,000</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program: Section 8 Housing Choice Vouchers	14.871		412,885
Pass-through the Commonwealth of Puerto Rico - Office of the Commissioner of Municipal Affairs: Community Development Block Grants - State's Program	14.228	05-AB 04-AB, FC-41 03-AB, FC-41 02-AB, FC-41 01-FD-41 00-FD-41 99-FD-41 98-FD-41 94-FD-41	<u>478,727</u>
Total U.S. Department of Housing and Urban Development			<u>891,612</u>
U.S. DEPARTMENT OF JUSTICE:			
Pass-through the Commonwealth of Puerto Rico - Department of Justice Edward Byrne Memorial Justice Assistance Grant Program	16.738	2005-DJ-00CVL-01	<u>34,237</u>
Total U.S. Department of Justice			<u>34,237</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2006

<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>
U.S. DEPARTMENT OF TRANSPORTATION:			
Pass-through the Commonwealth of Puerto Rico - Traffic Safety Commission			
State and Community Highway Safety	20.600	05-06-04 06-06-04	<u>125,779</u>
Total U.S. Department of Transportation			<u>125,779</u>
U.S DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico - Governor's Office (Elderly Office): Special Programs for the Aging - Title III, Part B, Grants for Supportive Services and Senior Centers	93.044	Not Available	103,372
Nutrition Services Incentive Program	93.053	Not Available	30,887
Pass-through the Commonwealth of Puerto Rico - Family Department (ADFAN): Community Service Block Grant	93.569	Not Available	30,112
Pass-through the Commonwealth of Puerto Rico - Family Department (ACUDEN): Child Care and Development Block Grant	93.575	Not Available	<u>184,936</u>
Total U.S. Department of Health and Human Services			<u>349,307</u>
U.S DEPARTMENT OF HOMELAND SECURITY:			
Pass-through the Commonwealth of Puerto Rico - Governor Authorized Representative (GAR): Predisaster Mitigation Competitive Grants	97.017	Not Available	37,305

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
Disaster Grants – Public Assistance	97.036	1247-DR-PR 1501-DR-PR 1552-DR-PR	43,772
Pass-through the Commonwealth of Puerto Rico – Emergency Management Agency Emergency Management Performance Grants	97.042	Not Available	4,189
Total U.S. Department of Homeland Security			85,266
TOTAL EXPENDITURES OF FEDERAL AWARDS			\$ 1,487,201

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, 2006

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 fund 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 Federal Grants and in the Other Governmental Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the fund financial statements and the expenditures in the Schedule of Expenditures of Federal Awards is as follows:

Description	Special Revenue Fund Federal Grants	Other Governmental Funds	Total
Per Schedule of Expenditures of Federal Awards	\$ 1,074,317	\$ 412,884	\$ 1,487,201
Non federal programs expenditures	<u>23,286</u>	<u>28,027</u>	<u>51,313</u>
Total expenditures in the general purpose financial Statements	<u>\$ 1,097,603</u>	<u>\$ 440,911</u>	<u>\$ 1,538,514</u>



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

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

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Luquillo, Puerto Rico**, as of and for the year ended June 30, 2006, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated November 28, 2006, which was unqualified. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Luquillo's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting 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 financial reporting that, in our judgment, could adversely affect **Municipality of Luquillo's** ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items **06-01** and **06-02**.

A material weakness is a reportable 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 caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs are not material weaknesses.

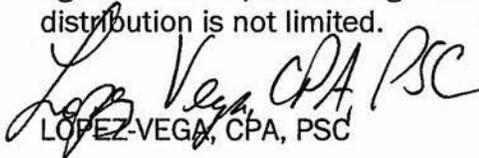
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS (CONTINUED)

Compliance and Other Matters

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

We noted certain other matters that we reported to management of the **Municipality of Luquillo** in a separate letter dated November 28, 2006.

This report is intended solely for the information and use of 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 28, 2006

Stamp No. 2196003 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



López-Vega, CPA, PSC

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**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, 2006. The **Municipality of Luquillo's** major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of 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.

In our opinion, 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, 2006. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items, **06-03 through 06-06**.

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

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 **06-03** and **06-05**.

A material weakness is a reportable 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 caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions, and accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weakness. However, of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs are not 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 13, 2007.

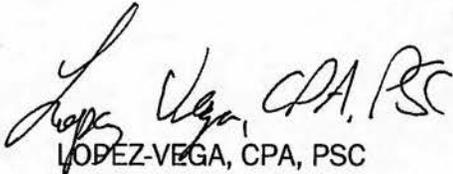


López-Vega, CPA, PSC

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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

San Juan, Puerto Rico
February 13, 2007

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López-Vega, CPA, PSC

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2006

Section I – Summary of Auditor’s Results

Financial Statements

Type of auditor’s report issued:	Unqualified	
Internal control over financial reporting:		
Material weakness identified?	Yes	No X
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	No X
Reportable conditions identified not considered to be material weaknesses?	Yes X	None reported
Type of auditor’s report issued on compliance for major programs:	Unqualified	
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 Grants – 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, 2006

Section II – Financial Statements Findings

Finding Reference	06-01
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).
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.
Questioned Cost	None
Management Response and Corrective Action	The Municipality registers all the transactions in a General Ledger using the Mechanized Accounting Uniform System (SUCH) provided by the Commissioner Officer for Municipal Affairs (OCAM). This system summarizes the entire Local, State and Federal Funds used regularly. In addition, the Municipality has finished the Work Schedule implanted by OCAM, in order to comply with all the procedures established by that Agency.

Implementation Date: March 15, 2007

Responsible Persons: Annette Caraballo – Finance Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section II – Financial Statements Findings

Finding Reference 06-02

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

Statement of Condition We performed a cash disbursement test and examined thirty one (31) disbursement vouchers which belonged to Community Development Block Grants – State Program, twenty (20) which belonged to Government Development Bank (GDB) Loan \$4,430,000 account, fifteen (15) which belonged to Joint Resolutions account, and nineteen (19) which belonged to Child Care Development Grant Program. The following will summarize the internal control exceptions noted:

- a. The Municipality did not reserve the necessary budgetary credits for the payment of services, at the time of formalizing contracts. (Seven (7) of these were related to the Community Development Block Grants – State Program, and five (5) related with the Joint Resolutions account.)
- b. Sixteen (16) disbursement vouchers did not have all of its supporting documents stamped as paid. (Nine (9) of these were related to the Community Development Block Grants – State Program, and two (2) related with the Joint Resolutions account.)
- c. Seven (7) disbursement vouchers were not available for our examination. (One (1) of these was related to the Joint Resolutions account, and six (6) related with the Government Development Bank (GDB) Loan \$4,430,000 account.

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. Also, Chapter Eight (8) establishes the procedures related to the quotations for the purchase of goods or services.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section II – Financial Statements Findings

Finding Reference	06-02 (Continued)
Cause of Condition	The Municipality internal control failed to assure that all transactions realized by the Municipality are supported by all the required documentation.
Effect of Condition	The Municipality is not in compliance with Chapter Four (4) and Eight (8) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.
Recommendation	We recommend to the Municipality's management to improve its internal control and procedures in order to assure that all disbursement vouchers are properly safeguarded, and to assure that disbursement vouchers includes all the required supporting documents before the issuance of any payment.
Questioned Cost	None
Management Response and Corrective Action	<p>The Municipality concurs with the findings. The following describes the actions taken by management:</p> <ul style="list-style-type: none">a. The Municipality had the necessary budgetary credits for the payment of all the contracts at the time of the formalization, but involuntary error between different departments did not allow reserving the credits on time. Actually, the Finance Director certifies the funds before the formalization of any contract. Secretarial Department is in charge of send a copy of the contract and supporting documents to Purchase Department in order to register the Purchase Order. <p>Implementation Date: March 2007</p> <p>Responsible Persons: Miss Carmen Velazquez - Municipal Secretary Mrs. Santa Diaz –Director of Purchasing Mrs. Annette Caraballo - Finance Director</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section II – Financial Statements Findings

Finding Reference 06-02 (Continued)

- b. The Finance Director has instructed the Official Payer to mark all the supporting documents as paid after printing the checks. Therefore, all the supporting documents of the disbursement indicated by the auditors have been marked as paid.

Implementation Date: March 2007

Responsible Person: Axel Dones, Official Payer

- c. The Finance Director has instructed the person in charge of filing disbursements documents to maintain all the supporting documents in order, so that they can be available to internal or external auditors.

Implementation Date: March 2007

Responsible Person: Carmen Benabe, Office Clerk

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	06-03
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Cash Management
Statement of Condition	We realized a Cash Management Test and after our procedures, we found that the Municipality maintained during the current fiscal year, average cash balance in books of approximately \$124,212. At June 30, 2006, the cash balance in book was \$118,303. Of these funds, \$2,967 was from operating reserve, \$44,435 was from Family Self Sufficiency's program (related to the balance not yet spent), \$5,509 was received from renter's frauds identified by the program, \$4,513 was from incorrect deposits by HUD, \$22,838 was from funds not used for Administrative fees, \$5,000 was from funds not used for Audit fees, \$160 was from accumulated interest and the remaining \$32,881 was not identified by us with respect to its origin.
Criteria	OMB Common Rules, Subpart C, Section 85.20 (b) (7), requires a cash management system; in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursement by the grantee.
Cause of Condition	The Municipality did not maintain appropriate cash management procedures in order to request funds to federal agencies only for immediate needs.
Effect of Condition	The PHA did not comply with the OMB Common Rules, Subpart C, Section 85.20, (b) (7).
Recommendation	We recommend to the Municipality's management to instruct the program accountant to review the accounting records and related transactions supporting documents for the current and past years in order to identify the cash balance respects to its origin, and later, to make any necessary adjusting journal entries to correct accounting records.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 06-03 (Continued)

Questioned Costs None

**Management Response
and Corrective Action** We will take the following measures to correct the finding: (a) We will notify to the responsible person to identify the remaining amount of \$32,881 and; (b) we will establish internal controls and procedures to avoid similar situations.

Implementation Date: March 2007

Responsible Person: Yazmin Maldonado - Accountant

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section III – Mayor Federal Award Program Finding and Questioned Cost

Finding Reference	06-04
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 (OCAM)
Requirement	Allowable Activities
Statement of Condition	<p>We performed a housekeeper activities test of seven (7) participant’s files and found the following exceptions:</p> <ul style="list-style-type: none">a) In six (6) participant’s files, there was no evidence the Service Coordinator visit at least two times per month the participant housing unit to ensure the quality of services.b) In one (1) participant’s file, there was no evidence of the approval form (OCAM-AH-004A);c) In five (5) participant’s files, there was no evidence of the participation contract between the Municipality and the participant, establishing the service plan to be offered (OCAM-AH-005).
Criteria	<p>Code of Federal Regulations 24, Section 570.484 states that the Municipality must assure that the program funds benefit very low, low- and moderate income persons and retain documentation justifying its certification. Also, the Municipality has an operational guide that includes all procedures and program’s requirements for housekeeper activities.</p>
Cause of Condition	<p>The Municipality’s controls and procedures failed to assure that the participant’s files include all the required documents to comply with the program requirements.</p>
Effect of Condition	<p>The Municipality is not in noncompliance with Code of Federal Regulations 24, Section 570.484 and with the operational guide.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference **06-04 (continued)**

Recommendation We recommended management to follow the procedures established in the operational guide title “Guía Operacional para la Prestación del Servicio de Auxiliares del Hogar”, including the use of the forms included on it.

Questioned Costs None

Management Response and Corrective Action We will take the following measures to correct the finding: (a) We will notify the responsible person to proceed according the established rules; (b) establish internal controls and procedures to detect missing documents and; (c) establish a quality control program.

Implementation Date: July 2006

Responsible Person: Nelson Márquez - Federal Program Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	06-05
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 (OCAM)
Requirement	Allowable Costs and Cost Principles
Statement of Condition	Section II – Financial Statement Findings – Finding Reference 06-02

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	06-06
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 (OCAM)
Requirement	Cash Management
Statement of Condition	During our cash management test, we noted that the Municipality requested funds that were not disbursed on a reasonable lapse of time. Also, the program cash account maintained a monthly average cash balance of \$71,608 in books.
Criteria	Code of Federal Regulations 24, Subpart I, Sec.570.489 (c), requires a cash management system in order to minimize the time elapsed between the transfer of funds from the pass-through grantor and disbursements made by the grantee.
Cause of Condition	The Municipality’s disbursements procedures failed to assure that funds requested and received from the Pass-through Grantor be disbursed in compliance with the Code of Federal Regulations Requirements.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Sec.570.489 (c).
Recommendation	We recommend management to strengthen it’s disbursement procedures to minimize the time elapsed between the transfer of funds from the Pass-through Grantor and the disbursements made by the Municipality.
Questioned Costs	None
Management Response and Corrective Action	The Municipality concurs with the finding. Management will take the following measures to correct the finding. Strengthen the internal controls and procedures for monitoring the cash balances monthly. Also, funds will be requested to the Pass-through Grantor only when needed, and disbursed promptly.

Implementation Date: March 2007

Responsible Person: Yazmin Maldonado - Accountant

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2006

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
05-03	14.871	<p><u>The Cash Management Test revealed that the Municipality maintained during fiscal year 2005-2006, average cash balance in books of approximately \$85,749. At June 30, 2005, the cash balance in book was \$75,663. Of these funds, \$2,967 was from operating reserve, \$31,500 was from Family Self Sufficiency's program (related to the balance not yet spent), and the remaining \$41,196 was not identified by us with respects to its origin.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-03.</p>
05-04	14.871	<p><u>The eligibility test of fifteen (15) participant files revealed the following exceptions: a) in one (1) case, the PHA paid an incorrect Housing Assistance Payment to the owner, as result, during the fiscal year 2004-2005, the program paid a HAP to the owner of \$3,489 instead of \$3,540; b) in four (4) cases, the PHA used an incorrect utility allowance for the HAP calculation and, in one (1) of these cases, an incorrect Fair Market Rent was used for the HAP calculation.</u></p> <p>Partial corrective action has been taken. The Municipality used the incorrect Fair Market Rent by a communication problem with San Juan HUD Office.</p>
05-05	14.871	<p><u>The reporting test revealed that the expenditures recorded in the Section 8 Housing Choice Vouchers program accounting records disagree with the Housing Assistant Payments and administrative expenditures reported in the Financial Quarterly Reports.</u></p> <p>Corrective Action was taken.</p>
05-06	14.871	<p><u>The PHA did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2005. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten percent or more in a utility rate.</u></p> <p>Corrective Action was taken.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
05-07	14.228	<p><u>The housekeeper activities test of six (6) participant's files revealed the following exceptions: a) in three (3) participant's files, there was no evidence of the copy of the social security; b) in one (1) participant's file, there was no evidence of the birth certificate; c) in one (1) participant's file, there was no evidence of the approval form (OCAM-AH-004A); d) in six (6) participant's files, there was no evidence of the participation contract between the Municipality and the participant, establishing the service plan to be offered (OCAM-AH-005).</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-04.</p>
05-08	14.228	<p><u>The cash disbursement test of twenty one (21) disbursement vouchers which belonged to Community Development Block Grants - State's Program revealed the following exceptions: a) in one (1) disbursement voucher, the purchase order was issued after the receiving of goods of services; b) one (1) disbursement voucher did not include the three (3) quotations required by law; c) ten (10) disbursement vouchers did not include all supporting document marked as paid.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-05.</p>
05-09	14.228	<p><u>The cash management test revealed that the Municipality requested funds that were not disbursed on a reasonable lapse of time. Also, the program cash account maintained a monthly average cash balance of \$82,364 in books.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-06.</p>
05-10	14.228	<p><u>The contract provision test of two (2) contracts for the Community Development Block Grants - State's Program, formalized during the fiscal year ended June 30, 2005, revealed the following situations: a) two (2) contracts did not include a provision for compliance with the Clean Air Act and Water Act; b) two (2) contracts did not include a provision for granting access to GAO or other Federally Agency, to books, documents, etc; c) two (2) contracts did not include a provision for compliance with Energy Policy and Conservation Act; d) two (2) contracts did not include provision for retention of all required records for three</u></p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<p><u>years; e) two (2) contracts did not include a provision for compliance with suspension and debarment.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-07.</p>
05-11	14.228	<p><u>The reporting requirements test of the Community Development Block Grants - State's Program revealed the following: a) differences between the amounts presented in the Financial Quarterly Reports and the amounts presented in the Program's General Ledger; b) the Financial Quarterly Report for the period ended December 31, 2004 was submitted to the Office of Commissioner of Municipal Affairs twenty three (23) days after the deadline; c) for the periods ended September 30, 2004 and March 31, 2005, there was no evidence of the submission date of the Financial Quarterly Reports to the Office of Commissioner of Municipal Affairs; d) Program year reports 2000 and 2003, included as part of the Financial Quarterly Report ended on June 30, 2005, have mathematical differences in the total column.</u></p> <p>Corrective Action was taken.</p>
04-02	14.871	<p><u>The PHA maintained, during the current fiscal year, average cash balance in books of approximately \$78,254. At June 30, 2004, the cash balance in book was \$63,385; \$3,495 of these funds was from HUD overpayment during the fiscal year 2003-2004 as determined in the preliminary year-end settlement; \$7,399 was from operating reserve at June 30, 2004; and the remaining \$52,491 was not identified with respects to its origin.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-03.</p>
04-04	14.871	<p><u>The PHA did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2004. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten percent or more in a utility rate.</u></p> <p>Corrective Action was taken.</p>
04-05	14.228	<p><u>Three (3) housekeeping assistance project participant's files did not have copy of the social security of the family members. Also, five (5) participant's files did not have complete evidence to support medical expenditures of the participant; eight (8) participant's files did not have</u></p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<p><u>evidence of the approval form (OCAM-AH-004A); eight (8) participant's files did not have the participation contract between the Municipality and the participant, establishing the service plan to be offered (OCAM-AH-005) and; in seven (7) cases, the Service Coordinator visited approximately one time every two month the participant house to ensure the quality of services. Also, the Service Coordinator did not use the OCAM-AH-006 when visited the participant housing unit.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-04.</p>
04-07	14.228	<p><u>Procurement test - Two (2) contracts did not include a provision for compliance with the Clean Air Act and Water Act; three (3) contracts did not include a provision for compliance with Energy Policy and Conservation Act and; one (1) contract did not include provisions for retention of all required records for three years.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 06-07.</p>
04-08	14.228	<p><u>Financial Quarterly Reports - several differences were found between the amounts presented in the Financial Quarterly Reports and the amounts presented in the program's General Ledger; three (3) of the Financial Quarterly Reports for the fiscal year 2003-2004 were submitted to the Office of Commissioner of Municipal Affairs after the deadline and; program year reports 2002, 2000 and 1994, included as part of the Financial Quarterly Report ended on March 31, 2004, have mathematical differences in the total column.</u></p> <p>Corrective Action was taken.</p>
04-09	93.575	<p><u>On fifteen (15) disbursement vouchers the Municipality did not cancelled or marked as paid the documents along the disbursements voucher; on one (1) disbursement vouchers there was no evidence of the original invoice; on two (2) disbursement vouchers there was no evidence of the receiving report or the certification of the Municipality's employee who receive of the good or services; on four (4) disbursement vouchers the Purchase Order was issued after the receiving of goods or services; nine (9) cancelled checks were not available for our examination.</u></p> <p>Corrective Action was taken.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
04-11	93.575	<p><u>No evidence was maintained of the submission by the Municipality of the Equipment Inventory and the Trial Balance as of September 30, 2003 and September 30, 2004, respectively. Also, no evidence was found of the submission date of the Annual Closing Report (CC-006) for the program fiscal years ended September 30, 2003 and September 30, 2004.</u></p> <p>No corrective action was taken. The Municipality submitted the documents after the due date.</p>
03-06	14.871	<p><u>In seven (7) participant's files the program used an incorrect utility allowance amount in the Housing Assistance Payment calculation. In eight (8) participant's files the program, as part of the Housing Assistance Payment calculation, did not used the lower of the "Payment Standard for the Family" or the "Gross Rent of the Unit". On ten (10) participant's files the Housing Assistance payment was incorrectly determined. As result, the program paid an incorrect Housing Assistance Payment to the owner and it cause differences in the amount of Tenant Rent to owner or the utility reimbursement to the family. In one (1) participant's file the final Housing Assistance Payment calculation reflect a HAP to owner of \$393 and a Tenant Rent to Owner of \$220. Those amount represents an over payment of \$56 because the rent to owner was only \$557. In one (1) participant's file the PHA did not reexamine a family income and composition reexamination during the fiscal year 2002-2003.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
03-07	14.871	<p><u>The PHA maintained during the current fiscal year average cash balance in books of approximately \$45,974. At June 30, 2003, the cash balance in book was \$64,958; \$23,959 of these funds was from HUD overpayment during the fiscal year 2002-2003 as determined in the year-end settlement; \$4,236 was from operating reserve at June 30, 2003, as determined in the year-end settlement; and the remaining \$36,763 the auditors could not determine its origin. Also, during seven months of the fiscal year 2002-2003 the PHA maintained a leasing rate under 95%, and maintained an average leasing rate of 94% for the fiscal year. The PHA did not submit to HUD a revised requisition (Form 52663) to reduce the monthly advances.</u></p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF LUQUILLO**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2006

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
03-09	14.871	<p><u>The PHA did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2003. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten percent or more in a utility rate.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>
03-12	14.228	<p><u>During the examination of reporting, the auditors verified the Financial Quarterly Report ended on June 30, 2003. They found differences between the amounts presented in the Financial Quarterly Report and the amounts presented in the program's General Ledger.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>