

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

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

OFICINA DEL COMISIONADO
DE ASISTENTES MUNICIPALES
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**MUNICIPALITY OF PATILLAS, PUERTO RICO
SINGLE AUDIT REPORT
JUNE 30, 2006
(INDEPENDENT AUDITOR'S REPORT)**

*Juan Feliciano Charneco * Certified Public Accountant*

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OFICINA DEL COMISIONADO
DE ASISTENTES MUNICIPALES

**MUNICIPALITY OF PATILLAS, PUERTO RICO
SINGLE AUDIT REPORT
JUNE 30, 2006**

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Estado Libre Asociado de Puerto Rico
Gobierno Municipal del Pueblo de Patillas

Sr. Narciso Velásquez Rodríguez
Finance Director

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Municipality of Patillas, we offer the reader of the Municipality's financial statements this narrative overview of the financial activities of the Municipality for the fiscal year ended June 30, 2006. We encourage readers to consider the information presented here in conjunction with the Municipality's financial statements.

Fiscal year 2005-2006 operations sustain the Municipality's track of solvency and sound fiscal condition. The Governmental Wide financial statement also supports our statement. This condition is achieved in a time of economy constrains and low revenues growth rates.

FINANCIAL HIGHLIGHTS

- The assets of the Municipality Government exceeded its liabilities at the close of the current fiscal year by \$8,973,702 (net assets).
- The adjusted actual of the General Fund operations resulted in a favorable variance of \$288,868 as compared to the revised budget.
- As June 30, 2006 the Municipality's General Fund (the primary operating fund) reported a fund balance of \$304,421 a decrease of \$141,534 in comparison with the prior year.
- Loans principal payments were \$369,750 during fiscal year 2005-06. Loan proceeds from new debt issued amounted to \$1,234,000 during the same fiscal year.
- During fiscal year 2005-2006 the General Fund received a reduction of approximately \$208,000, related with remittances from CRIM due to the temporary central government closure.

New Requirements for the Financial Reporting

The new approach on the preparation of the Municipality's financial statements emphasizes on a government wide (consolidated) view of its financial operations. Nevertheless major individual funds are presented and evaluated in all of its details. Simultaneous implementation of both of these perspectives allows user to address relevant questions about municipality's performance and provides a basis for comparisons and evaluation of services quality.

MUNICIPALITY OF PATILLAS MANAGEMENT'S DISCUSSION AND ANALYSIS

Because of the implementation of these new reporting standards, much of the information will not be easily comparable with prior year data. However, in future years, comparisons will be more meaningful and will provide a better understanding of the municipality's financial position and results of its operations.

Financial Statements Components

The basic financial statement consist of government wide financial statements, the major individual funds financial statement, and notes to the financial statements that provides more details.

The Statement of Net Assets reports information of the municipality as a whole. Increase or decrease of net assets may serve as an indicator of whether municipality's financial position is improving or deteriorating. Those statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private sector companies. Accrual of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The statement of Activities is focused on both the gross and net cost of various activities, which are supported by the Municipality's property tax, municipal licenses tax and other revenues. It is intended to summarize and simplify the user's analysis of the costs of governmental services. The governmental activities reflect basic services, including police, public works, solid waste disposal, community services, and general administration. Property tax, municipal license tax, state and federal appropriations finance most of the services.

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Major Governmental Funds presentation provides detailed information about the most significant funds, not the Municipality as a whole. The Municipality uses fund accounting to ensure and demonstrate compliance with financial related legal requirements. The Municipality's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The Governmental funds statement provides a detailed short-term view of the Municipality general governmental operations and the basic services it provides. Governmental funds information help you determine whether there are more or fewer financial resources that can be spend in the near future to finance Municipality's programs. We describe the relationship between governmental activities and governmental funds in reconciliation besides the fund financial statements.

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statement.

**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Infrastructure Assets

The Municipality implemented the major model portions of GASB statement 34 during the current fiscal year. Historically, the governmental larger group of assets have not been reported nor depreciated in governmental financial statement. The new statement required that this asset be valued and reported within the Governmental column of the Governmental Wide Statement. Additionally, the government must elect to either depreciate these assets over their estimated useful life or develop a system of assets management designated to maintain the service delivered potentially to near perpetuity. If the government develops the assets management system, which periodically, by category, measures and demonstrate its maintenance system, which periodically, by category, measures and demonstrate its maintenance of locally established level of services standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statements users in evaluating a local government and its performance over time.

The Municipality has not recorded the infrastructure assets from prior year and will comply with GASB Statement 34 before 2006-07.

Government-Wide Statement

Statement of Net Assets

The Statement of Net Assets reports information of the municipality as a whole. Increase or decrease of net assets may serve as an indicator of whether municipality's financial position is improving or deteriorating. In the case of the Municipality primary government assets exceeded liabilities by \$8,973,702 at the close of the recent fiscal year. The following reflects the condensed Statement of Net Assets of the Primary Government.

**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

**Statements of Net Assets
As of June 30, 2006 and 2005**

	2006	2005
Current and other assets	\$4,948,127	\$3,976,019
Capital assets	12,906,421	10,658,921
Total assets	<u>\$17,854,548</u>	<u>\$14,634,940</u>
Current and other liabilities	\$3,000,553	\$ 2,396,111
Long-term liabilities	<u>5,880,293</u>	<u>5,495,281</u>
Total liabilities	8,880,846	7,891,392
Net assets:		
Invested in capital assets, net of related debt	8,648,954	4,484,002
Debt service	956,599	1,043,291
Special and other funds	363,265	278,855
Capital project fund	1,250,053	491,445
Unrestricted (deficit)	(2,245,199)	445,955
Total net assets	<u>\$8,973,702</u>	<u>\$ 6,743,548</u>

The principal increase of the net assets was due mainly to the inclusion of the capital assets of the municipality. The Capital Assets' amount will increase as the infrastructure assets are identified and included in the financial statements.

Statements of Activities

The following reflects the condensed Statement of Activities of the Primary Government:

For the year ended June 30, 2006 and 2005

	2006	2005
General revenue	\$9,057,875	\$ 8,622,718
Program revenue	<u>3,288,375</u>	<u>3,369,600</u>
Total revenue	<u>12,346,250</u>	<u>11,992,318</u>
Expenses		
Governmental activities	10,912,644	12,926,130
Change in net assets	<u>\$1,433,606</u>	<u>\$ (933,812)</u>

**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

The following reflects the condensed Balance Sheet of the Governmental Funds:

**Governmental Funds
Balance Sheets
June 30, 2006 and 2005**

	2006	2005
Assets:		
Cash	\$1,596,031	\$ 2,025,979
Restricted Cash	2,997,368	1,043,291
Accounts Receivable	1,933,765	2,271,782
Total Assets	\$6,527,164	\$ 5,341,052
Liabilities and Fund Balance		
Liabilities:		
Total liabilities	\$3,157,441	\$ 3,081,506
Fund Balances	3,369,723	2,259,546
Total liabilities and Fund Balances	\$6,527,164	\$ 5,341,052

The most significant changes in this statement were as follows:

- Noticeably, the fund balances are mostly in cash and cash restricted.
- The increase in liabilities is due mainly to the accounts payable of special and capital projects funds.

**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

**Statement of Revenues, Expenditures and Changes in Fund Balances
Year Ended June 30, 2006 and 2005**

	2006	2005
Revenues:		
Property taxes	\$1,487,869	\$ 1,631,440
Volume of business tax	531,386	404,383
Intergovernmental revenue	5,323,831	4,836,599
Federal grants	2,697,496	3,595,969
Other	830,471	2,423,817
Total Revenues	10,871,053	12,892,208
Liabilities and Fund Balance		
Expenditures:		
General Government	3,752,664	3,960,725
Public safety and public work	2,408,473	3,522,790
Education and training and culture	1,539,457	1,215,573
Capital projects	1,193,139	2,622,090
Other	1,379,688	1,461,026
Bonds, notes and interests	576,049	501,027
Total Expenditures	10,849,470	13,283,231
Excess of revenues (expenditures)		
Over expenditures (revenues)	\$21,583	\$ (391,023)

The most significant changes of this statement were as follows:

- The larger decrease in revenues is related to other revenue for the amount of \$1,593,346.
- The most significant change in the expenditures were an increase in capital project for approximately \$1.2 millions related with capital outlays.

**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Economic Factors and Next Year Budget

The Municipality is a political legal entity with full legislative and administrative powers in every area of municipal government, with perpetual existence and legal personality, separate and independent from the central governmental of Puerto Rico. The Municipal Government comprises the executive and legislative branches. The Mayor exercises the executive power and the legislative power by the Municipal Legislature, which has 14 members.

The Municipality provides a full range of services including public works, education Public safety, public housing, health, community development, culture, recreation and other administrative services. The Municipality's principal sources of revenues are property taxes, municipal license taxes, contributions by the state government and federal grants.

The Municipality's Budget for fiscal year 2005-2006 is \$131,792 less than last fiscal year (2004-2005).

Contacting the Municipality's Financial Management

The Municipality's financial statements are designed to present users with general overview of the Municipality's finances. If you have questions about the report or need additional financial information, contact the Municipality's Director of Finance.


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INDEPENDENT AUDITOR'S REPORT

To the Mayor and Municipal Council of the Municipality of Patillas
Patillas, Puerto Rico

I have audited the accompanying financial statements of the Governmental Activities, each major fund and the remaining fund information of the **Municipality of Patillas**, Puerto Rico, as of and for the year ended June 30, 2006, which collectively comprise the **Municipality of Patillas** basic financial statements, as listed in the accompanying table of contents. These financial statements are the responsibility of the Municipality's management. My responsibility is to express opinions on these financial statements based on my audit.

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

In my 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 Patillas**, Puerto Rico, as of June 30, 2006, and the respective changes in financial position, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, I have also issued my report dated November 8, 2006 on my consideration of the **Municipality of Patillas**, Puerto Rico internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts and grants. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the result 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 and audit performed in accordance with Governmental Auditing Standards and should be considered in assessing the results of our audit.

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

As described in Note 1, on July 1, 2004, **the Municipality** implemented a new financial reporting model required by GASB Statement No. 34, (GASB No. 34), *Basic Financial Statements – And Management’s Discussion and analysis-for State and Local Governments*. In conjunction with the adoption of GASB No. 34, the Municipality has also adopted the following pronouncements: (1) GASB Statement No. 37-*Basic Financial Statements-and Management’s Discussion and Analysis-for State and Local Governments: Omnibus*, (2) GASB Statement No.38-*Certain Financial Statement Note Disclosures*, and (3) GASB Interpretation No. 6-*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*.

The Management’s Discussion and Analysis and budgetary comparison information on pages 1 through 7 and page 15, are not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. I 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, I did not audit the information and express no opinion on it.

San Juan, Puerto Rico
November 8, 2006

The stamp number
was affixed to the
original of this report

2171642

Juan A. Feliciano Charneco
CPA JUAN A. FELICIANO CHARNECO
License No. 1263
Expires December 1, 2007



MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF NET ASSETS
JUNE 30, 2006

	Governmental Activities
<u>ASSETS</u>	
Cash and investments	\$ 1,596,031
Cash with fiscal agent and other	2,997,368
Accounts receivable federal government	275,532
Accounts receivable government	79,196
Capital assets	12,906,421
Total assets	17,854,548
 <u>LIABILITIES AND FUND EQUITY</u>	
Liabilities:	
Accounts payable and accrued liabilities	670,956
Due to government entity	388,010
Deferred revenue	519,438
Noncurrent liabilities:	
Due within one year	1,422,149
Due in more than one year	5,880,293
Total liabilities	8,880,846
 <u>NET ASSETS</u>	
Invested in capital assets, net of related debt	8,648,984
Restricted for:	
Debt service	956,599
Special and other fund	363,265
Capital project fund	1,250,053
Unrestricted (Deficit)	(2,245,199)
Total net assets	8,973,702
Total Liabilities and net Assets	\$ 17,854,548

See notes to financial statement.

MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENTS OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

Functions/Programs	Expenses	Program Revenues			Net (expense) revenue and change in Net Assets in Governmental Activities
		Charges for Services	Capital Grants and Contributions	Operating Grants and Contributions	
<u>EXPENDITURES:</u>					
General government	\$ 3,774,633	\$ -	\$ (588,896)	\$ (584,632)	\$ 2,601,105
Public safety	545,126	-	-	-	545,126
Public works	2,228,905	(4,327)	-	-	2,224,578
Capital projects	1,193,139	-	(838,438)	(354,701)	-
Health	545,834	-	-	-	545,834
Culture and recreation	661,835	-	-	-	661,835
Other expenditures	839,492	-	-	-	839,492
Education and training	917,381	-	-	(917,381)	-
Interest on long-term debt	206,299	-	-	-	206,299
Total governmental activities	<u>10,912,644</u>	<u>(4,327)</u>	<u>(1,427,334)</u>	<u>(1,856,714)</u>	<u>7,624,269</u>
<u>GENERAL REVENUES:</u>					
Property taxes					\$ 1,487,869
Municipal licenses tax					531,386
Licenses, permits and fines					327,291
Intergovernmental revenues					5,323,831
Rent of properties					86,511
Interest revenues					14,032
Other revenues					985,230
Special item - Gain on sale of land					301,725
Total general revenues					<u>9,057,875</u>
Changes in net assets					1,433,606
Net assets at beginning of year					6,743,548
Prior period adjustment					796,548
Net assets at end of year					<u>\$ 8,973,702</u>

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2006

ASSETS	General Fund	2004 and 2005 Bonds Issue Fund	HUD Programs	Head Start Programs	Debt Service Fund	Other Funds	Total Governmental Funds
Cash and investments	\$ 1,327,381	\$ -	\$ 152,894	\$ 7,182	\$ -	\$ 111,574	\$ 1,599,031
Cash with fiscal agent and other	-	2,040,769	-	-	956,599	-	2,997,368
Accounts receivable federal government	-	-	114,932	136,420	-	21,180	272,532
Due from other funds	649,592	-	-	-	-	1,008,641	1,658,233
Total assets and other debits	<u>\$ 1,976,973</u>	<u>\$ 2,040,769</u>	<u>\$ 267,826</u>	<u>\$ 143,602</u>	<u>\$ 956,599</u>	<u>\$ 1,141,395</u>	<u>\$ 6,527,164</u>

LIABILITIES AND FUND BALANCES

Liabilities:							
Accounts payable and accrued liabilities	\$ 310,669	\$ -	\$ 77,164	\$ 143,602	\$ -	\$ 139,521	\$ 670,956
Due to special revenue funds	533,641	475,000	-	-	-	-	1,008,641
Due to general fund	-	-	10,983	-	-	638,609	649,592
Due to government entity	388,010	-	-	-	-	-	388,010
Deferred revenue	440,242	-	-	-	-	-	440,242
Total liabilities	<u>1,672,562</u>	<u>475,000</u>	<u>88,147</u>	<u>143,602</u>	<u>-</u>	<u>778,130</u>	<u>3,157,441</u>
Fund balances:							
Reserve for debt services	45,500	-	-	-	956,599	-	1,002,099
Encumbrances	-	-	-	-	-	-	-
General Fund	258,911	495,395	-	-	-	-	754,306
Special and other funds	-	-	-	-	-	363,265	363,265
Capital project fund	-	1,070,374	179,679	-	-	-	1,250,053
Total fund balances	<u>304,411</u>	<u>1,565,769</u>	<u>179,679</u>	<u>-</u>	<u>956,599</u>	<u>363,265</u>	<u>3,369,723</u>
Total liabilities and fund balance	<u>\$ 1,976,973</u>	<u>\$ 2,040,769</u>	<u>\$ 267,826</u>	<u>\$ 143,602</u>	<u>\$ 956,599</u>	<u>\$ 1,141,395</u>	<u>\$ 6,527,164</u>

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
 Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the funds:
 Accrued compensated absence
 Liability for claims and judgments
 Health insurance debt
 Bonds payable

	12,906,421
	\$ 704,191
	354,000
	1,011,814
	5,232,437
	<u>\$ 7,302,442</u>
	<u>7,302,442</u>
	<u>\$ 8,973,702</u>

Total net assets of governmental activities

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	General Fund	2004 Bonds issue Fund	HUD Programs	Head Start Program	Debt Service Fund	Other Funds	Total Governmental Funds
REVENUES:							
Property taxes	\$ 1,161,575	\$ -	\$ -	\$ -	\$ 326,294	\$ -	\$ 1,487,869
Municipal license tax	531,386	-	-	-	-	-	531,386
Licenses, permits and fines	327,291	-	-	-	-	-	327,291
Intergovernmental revenues	4,737,279	-	-	-	-	586,552	5,323,831
Rent of properties	86,511	-	-	-	-	-	86,511
Interest income	11,630	-	-	-	29,372	-	41,002
Other revenues	375,667	-	-	-	-	-	375,667
Federal financial award	-	-	1,427,334	917,381	-	352,781	2,697,496
Total revenues	7,231,339	-	1,427,334	917,381	355,666	939,333	10,871,053
EXPENDITURES:							
Current:							
General government	2,867,360	-	548,439	-	-	316,865	3,752,664
Public safety	516,385	-	-	-	-	-	516,385
Public works	1,892,088	-	-	-	-	-	1,892,088
Health	540,196	-	-	-	-	-	540,196
Capital projects	-	-	838,438	-	-	354,701	1,193,139
Culture and recreation	622,076	-	-	-	-	-	622,076
Other Expenditures	839,492	-	-	-	-	-	839,492
Education and training	-	-	-	917,381	-	-	917,381
Debt service:							
Principal retirement	-	-	-	-	369,750	-	369,750
Interest and fiscal charges	-	-	-	-	206,299	-	206,299
Total expenditures	7,277,597	-	1,386,877	917,381	576,049	691,566	10,849,470
Excess of revenues over (under) expenditures	(46,258)	-	40,457	-	(220,383)	247,767	21,583
Other financing source (uses):							
Transfer in (out) to debt service fund	(160,662)	-	-	-	160,662	-	-
Interest expenditure	-	-	-	-	(26,970)	-	(26,970)
Net bond issued debt	-	1,225,053	-	-	-	-	1,225,053
Bond Expenditure	-	(532,886)	-	-	-	-	(532,886)
Total other financing source (uses)	(160,662)	692,167	-	-	133,692	-	665,197
Excess of revenues and other sources over (under) expenditures and other uses	(206,920)	692,167	40,457	-	(86,691)	247,767	686,780
SPECIAL ITEMS:							
Proceeds from Sale of land	405,000	-	-	-	-	-	405,000
Net change in fund balances	198,080	692,167	40,457	-	(86,691)	247,767	1,091,780
Fund balance June 30, 2005	445,955	62,494	230,575	93,895	1,043,290	383,336	2,259,545
Prior period adjustment	(339,624)	811,108	(91,353)	(93,895)	-	(267,838)	18,398
Fund balance June 30, 2006	\$ 304,411	\$ 1,565,769	\$ 179,679	\$ -	\$ 956,599	\$ 363,265	\$ 3,369,723

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See notes to financial statements.

**MUNICIPALITY OF PATILLAS
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
JUNE 30, 2006**

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

Net change in fund balance - total governmental funds	\$ 1,091,780
---	---------------------

Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Expenditures for capital assets	1,193,139	
Less: current year depreciation	<u>(432,924)</u>	
		760,215

The gain on the sales of the land is reported, whereas in the governmental funds, proceeds from, the sales increase financial resources. Thus, the change in net assets differs from change in fund balance by the cost of the land sold.

103,275

The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets.

Net bond proceeds of bond issue	(1,225,053)	
Principal payments	369,750	
Bond expenditure	532,886	
Transfer to debt service	<u>(160,662)</u>	
		(483,079)

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

(38,585)

Change in net assets of governmental activities	\$ 1,433,606
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MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL (BUDGET BASIS)
GENERAL FUND AND DEBT SERVICE
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

	Budgeted Amounts		Adjusted Actual Note 1	Variance Favorable (Unfavorable)
	Original	Final		
REVENUES:				
Property taxes	\$ 298,686	\$ 298,686	\$ 298,686	\$ -
Municipal license tax	528,500	525,000	507,643	(17,357)
Intergovernmental revenues	4,964,841	4,964,841	4,791,776	(173,065)
Licenses, permits and fines	369,000	369,000	327,291	(41,709)
Rent of properties	75,000	75,000	86,510	11,510
Interest income	500	4,000	16,663	12,663
Other revenues	210,500	550,124	780,666	230,542
Other sources	862,888	862,888	862,888	-
Property tax (debt service)	306,307	442,357	314,948	(127,409)
Total revenues	\$ 7,616,222	\$ 8,091,896	\$ 7,987,071	\$ (104,825)
EXPENDITURES:				
Current:				
General government	\$ 2,584,201	\$ 3,047,448	\$ 2,901,062	\$ 146,386
Public safety	560,984	527,608	522,656	4,952
Public Work	2,846,705	2,633,530	2,604,528	29,002
Health	581,525	584,158	540,195	43,963
Culture and recreation	565,337	685,632	631,568	54,064
Other Expenditure	-	-	-	-
Transfer to debt service	171,163	171,163	160,662	10,501
Principal and interest	306,307	442,357	442,357	-
Total expenditures	\$ 7,616,222	\$ 8,091,896	\$ 7,803,028	\$ 288,868
Excess of revenues over (under) expenditures			\$ 184,043	\$ 184,043
Explanation of differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				<u>\$ 7,987,071</u>
Differences - budget to GAAP:				
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes.				59,432 (54,498)
Total revenues as reported on the statement of revenue, expenditure, and changes in fund balances				<u>\$ 7,992,005</u>
Uses/outflow of resources				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				<u>\$ 7,803,028</u>
Differences - budget to GAAP:				
Non budgeted expenditures				235,257
Budgeted expenditures included prior year				(157,669)
Other financial resources transferred to debt service				(26,790)
Total expenditures as reported on the statement of revenue, expenditures and change in fund balances				<u>\$ 7,853,826</u>

See notes to budgetary comparison schedule.

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
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JUNE 30, 2006

GENERAL ORGANIZATION

The **Municipality of Patillas (The Municipality)** was founded in 1811. The governmental system of the Municipality is composed of the executive and legislative bodies. The Mayor is the Chief Executive Officer and is elected every four years in the general elections of Puerto Rico. The legislative body consists of fourteen assemblymen also elected in the general elections of Puerto Rico for a four-year period.

The Municipality provides services such as: health, public safety, sanitation, recreation and sports, education, housing, transportation, welfare, construction and/or improvements of highways and streets, and other general and administrative services.

The financial statements of **the Municipality** have been prepared in conformity with generally accepted accounting principles (GAAP) as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the primary standard-setting body for establishing governmental accounting and financial reporting principles. The GASB periodically updates its existing Governmental Accounting and Financial Reporting Standards, which along with subsequent GASB Pronouncement (Statements and Interpretations,) institute GAAP for governmental units. A summary of **the Municipality's** significant accounting policies consistently applied in the preparation of the accompanying basic financial statements follows:

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Reporting Entity

The Municipality's financial statements include the operations of all departments and separate legal entities for which **the Municipality** is financially accountable or for which exclusion would leave the financial statements misleading or incomplete.

In June 1999, the GASB issued Statement No. 34 *Basic Financial Statements and Management Discussion and Analysis for State and Local Governments*. This statement establishes new financial reporting requirements for state and local governments. It requires new information and restructures much of the information that governments have reported in the past. Comparability with reports issued in prior years is affected. In June 2001, the GASB issued Statement No. 37 *Basic Financial Statements and Management Discussion and Analysis for State and Local Governments Omnibus*, which in part addressed the Management Discussion and Analysis (MD&A) requirements, Program Revenue Classifications and Major Fund criteria requirements in the reporting model in Statement No. 34.

The Municipality was required to implement this Standard for the fiscal year ended June 30, 2004.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
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b. Financial Reporting Entity

The accompanying basic financial statements include all departments, agencies and municipal entities that: (1) are under the legal and administrative control of the Mayor, and (2) whose funds are under the legal custody and control of **the Municipality's** Director of Finance, as prescribed by Law No. 81 of August 30, 1991, as amended, known as the *Autonomous Municipalities Act of the Commonwealth of Puerto Rico*. **The Municipality's** management has considered all potential component units for which it may be financially accountable and other legally separate organizations for which the nature and significance of their relationship with **the Municipality** may be such that exclusion of their financial statements from those of the Municipality would cause **the Municipality's** basic financial statements to be misleading or incomplete according to GASB Statement No. 14, - *The Financial Reporting Entity (GASB No. 14.)*

The Municipality's management has concluded that, based on the aforementioned criteria, there are no legally separate entities or organizations that should be reported as component units of **the Municipality** as of June 30, 2006 nor for the year then ended.

c. Basic Financial Statements-GASB Statement No. 34

The basic financial statements include both government-wide and fund financial statements. While the previous model emphasized fund types (the total of all funds of a particular type), in the new reporting model the focus is on major individual funds (within the fund financial statements). Both the government-wide and fund financial statements categorize activities as governmental activities. In the government-wide Statement of Net Assets the governmental activities (a) are presented on a consolidated basis in one column, and (b) are reflected, on a full accrual, economic resource basis, which incorporates long-term assets and receivables as well as long-term debt and obligations.

The Government-wide Statement of Activities reflects both the gross and net cost per functional category. The Statement of Activities reduces gross expenses (including depreciation) by related operating grants and contributions. The operating grants include operating-specific grants.

This government-wide focus is more on the substantiality of **the Municipality** the change in aggregate economic position resulting from the activities of the fiscal period.

The fund financial statements are, in substance, very similar to the financial statements presented in the previous model. Emphasis here is on the major funds in the governmental category. Non-major funds are aggregated into a single column.

MUNICIPALITY OF PATILLAS, PUERTO RICO
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The governmental funds financial statements are presented on a current financial resource measurement focus and modified accrual basis of accounting. This is the manner in which these funds are normally budgeted. This presentation is deemed most appropriate to (a) demonstrate legal and covenant compliance, (b) demonstrate the source and use of liquid resources, and (c) demonstrate how **the Municipality** actual experience conforms to the budget or fiscal plan. Since the governmental fund statements are presented on a different measurement focus and basis of accounting than the government-wide statement, a reconciliation is presented on the fund statement, which briefly explains the adjustments necessary to transform the fund statements into the governmental wide statements.

d. Basis of Presentation

The new model as defined in Statement No. 34 establishes criteria (percentage of the assets, liabilities, revenues or expenditures/expenses of either fund category or the governmental and enterprise combined) for the determination or major funds. **The Municipality** reports the following major funds on **Fund Financial Statements**:

Major Funds

General Fund – Always a major fund. The general fund is the main operating fund of **the Municipality**. It is used to account for all financial resources except those required to be accounted for in another funds.

HUD Programs Fund – This fund accounts for revenues sources for the development of viable urban communities, decent housing suitable living environment, rental assistance to help very low-income families afford decent, safe and sanitary housing by encouraging property owners to rehabilitate substandard housing and lease the units with rental subsidies to low income families.

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

Head Start – Program Funds – The special revenue fund of Head Start is a major fund used by **the Municipality** to account for revenues derived from the grant that is legally restricted by outside parties for use on specific purpose. The uses and limitations of this revenue fund are specified by municipal ordinances of federal and state statutes.

However, resources restricted to expenditure for purposes normally financed from the general fund are reported in **the Municipality's** general fund provided that all applicable legal requirements are appropriately satisfied. In this case, a special revenue fund to account for such kind of transactions will be used only if legally mandated.

MUNICIPALITY OF PATILLAS, PUERTO RICO
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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

d. **Basis of Presentation (continuation)**

Other Funds (not major funds) – Special revenue funds are used to account for the proceeds of specific revenues sources that are legally restricted to expenditures for specified purposes. Capital projects fund is used to account for the financial resources for the acquisition of personal property and/or construction of major improvements, which are not financed by other funds.

e. **Basis of Accounting**

The accounts of **the Municipality** are organized on the basis of funds, each of which is considered to be a separate accounting entity. **The Municipality** has created various types of funds. Each fund is accounted for by a separate set of self-balancing accounts, which include its assets, liabilities, fund balances, and revenues and expenditures/expenses, as applicable. The individual funds accounts for the governmental resources allocated to **the Municipality** for the purpose of carrying on specific activities in accordance with laws, regulations, or other restrictions.

Measurement Focus, Basis of Accounting

Government-wide Financial Statements – The government wide financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Non-exchange transactions, in which **the Municipality** gives (or receives) value without directly receiving (or giving) equal value in exchange, include grants. Revenue from grants is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Governmental Funds Financial Statement – Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. Available means collectible within the current period or 60 days after the end of the period to use them to pay liabilities of the current period. Miscellaneous revenues are recorded when collected. Revenues collected in advance of the fiscal year to which they apply are recorded as deferred revenues and recognized as revenues in the year to which they apply. Expenditures are generally recognized when the related fund liability is incurred. General capital asset acquisitions are reported as expenditures in governmental funds.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

e. **Basis of Accounting** (Continuation)

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

Licenses and permits, charges for services, fines and forfeits and miscellaneous revenues (except investment earnings) are recorded as revenues when received. Investment earnings (interest) are recorded as earned since they are measurable and available.

f. **Encumbrances**

Governmental funds employ encumbrances accounting. Under the encumbrance system, all purchase orders; contracts and other commitments for the expenditure of funds are recorded in order to reserve that portion of the applicable appropriation. Under generally accepted accounting principles, encumbrances outstanding at year-end are reported as reservations of fund balance and they constitute neither expenditures, nor liabilities. Encumbrances constitute the equivalent of expenditures for budgetary purposes only, and accordingly, are reported with expenditures in all budgetary basis statements.

g. **Budgetary Data**

The Municipality follows these procedures, which are in accordance with the municipal law; in establishing the budgetary date reflected in the basic financial statements.

- (1) On or prior to May 15, the Mayor submits to the Municipal Assembly a proposed budget for the fiscal year commencing the following July 1st. The proposed budget includes estimated expenditures and their financing sources.
- (2) The budget document is available for public inspection prior to its approval by the Municipal Assembly.
- (3) Prior to July 1st., the annual budget is legally enacted through passage of the annual appropriation ordinance.
- (4) Subsequent to the enactment of the annual appropriation ordinance, the Municipal Assembly has the authority to make necessary adjustments to the budget.

The budget is prepared following the modified accrual basis of accounting except for the encumbrances, as described below:

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

g. **Budgetary Data** (Continuation)

The actual results of operations, presented in the Statement of Revenues, Expenditures and Changes in Fund Balances-Budget and Actual-General Fund, are reflected in conformity with the budgetary accounting of the Municipality for a better comparison with the budget information.

Amendments to the budget, and budgetary transfers related to personal expenditures, require the approval of the Municipal Assembly. Non-capital encumbrances lapse at the end of the next fiscal year. During the fiscal year, the Municipality readjusted its original budget of the General Fund Balance by \$475,674 from current year resources increase.

Since the budgetary basis differs from generally accepted accounting principles (GAAP), actual amounts for the general fund and debt service fund in the accompanying Statement of Revenues and Expenditures-Budget and Actual are presented on the budgetary basis to enhance comparability. The principal differences are as follows:

- (1) Encumbrances are recorded as expenditures under the budgetary basis and as reservations of fund balance under the GAAP basis.
- (2) The property tax advances are presented as revenue in the budgetary basis and as other financing sources in the GAAP basis.
- (3) The Municipality receives certain revenues as contributions from governmental entities, legislative and private parties, which are not included therein nor are the related expenditures.
- (4) Certain debt issuance to acquire personal property is reflected in the general fund and is restricted for that purpose

The Municipality has not legally adopted a budget for the Head Start special revenue and capital projects funds. Accordingly, it has not presented an annual comparison of budget and actual for these major funds.

MUNICIPALITY OF PATILLAS, PUERTO RICO
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h. Deposits

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

i. Inventories

The general fund purchases office and printing supplies, gasoline, oil, medicines and other items. The cost of purchases is recorded as a expenditures and the inventory is not recorded in the basis financial statements since amount is insignificant.

j. Capital Assets

Fund Financial Statements

The capital assets acquired are recorded as expenditures at cost in the governmental funds.

Government Wide Financial Statement

Purchased capital assets are recorded at cost. Donated capital assets are recorded at their estimated fair value a time they are received by **the Municipality** and is capitalized in the Statement of net Assets. Major renewals and betterment are capitalized: replacement, maintenance and repairs, which do not improve or extend the life of the respective assets, are charged to operations.

Depreciation is provided over the estimated useful life of the respective assets on straight-line basis.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
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k. Vacation and Sick Leave and Other Compensated Absences

Municipal employees are granted 30 days of vacation and 18 days of sick leave annually. Vacation may be accumulated up to a maximum of 60 days and sick leave up to a maximum of 90 days. In the event of employee resignation, the employee is paid for accumulated vacation days up to the maximum allowed. Separation from employment prior to use of all or part of the sick leave terminates all rights for compensation, except for employees with ten years or more of service who are entitled to sick leave pay to the maximum allowed. The Municipality is required to pay excess sick leave over 90 days on or before March 31 of the accumulated excess at December 31 of prior year. Employees' maximum allowed accumulated vacation, with the employer's share of payroll taxes, are accounted in for the Statement of Net Asset.

l. Insurance

The Municipality has insurance coverage for its public facilities and equipment, primarily to provide protection in case of disaster and other losses. Also, principal officials of **the Municipality** are covered under various surety bonds. The Secretary of the Department of the Treasury of the Commonwealth of Puerto Rico is the designated agency to obtain the necessary insurance coverage for **the Municipality**.

m. Restricted Assets

Investments and Certificates

Certain proceeds of as well as certain resources set aside for their repayment are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants. The "revenue bond" maintenance account is used to report those rental proceeds that are restricted for use in maintenance of the properties. The "revenue bond fund account" is used to segregate resources accumulated for debt service payments over the next twelve months. The "Debt Service Account" is used to report resources set aside to make up potential future deficiencies in the "revenue bond fund account".

Cash with fiscal agent

The cash with fiscal agent pertaining to the debt service represents property tax collections retained by the Government Development Bank for Puerto Rico and another financial institution restricted for the payment of **Municipality's** debt service (See Note 2) and unused proceeds from bonds and notes issued principally for the acquisition or construction of permanent improvements are accounted in the capital project fund.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
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n. Reservations of Fund Balance

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

- *Encumbrances* – Represent future expenditures under purchase order, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
- *Debt Service* – Represents net assets available to finance future debt service payments.
- *Capital Projects* – Represent net assets available to finance future capital outlays.
- *Special Revenue Fund* – Represent net assets available to finance specified outlays.
- *General Fund* – Represent net assets available not required to be accounted in another fund.
- *For other Purposes* – Represent mainly resources set aside for use in federal and state grant programs accounted for in the special revenue funds, and resources available in the general fund for the payment of certain accounts payable and commitments approved by GDB.

o. 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 and in the Statement of Net Assets.

p. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that effect the reported amounts of assets and liabilities and disclosure of contingent 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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
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q. Totals Column (Memorandum Only) Governmental Funds Statement

The total data under this column is presented only to facilitate financial analysis. Data in these columns do not present financial position or results of operations in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation, since Interfund eliminations have been made.

2. PROPERTY TAXES

The “Centro de Recaudación de Ingresos Municipales”(CRIM) is responsible for the assessment of all real and personal property located within the **Municipality of Patillas** and for the levy, administration and collection of the corresponding taxes.

The property tax is levied each year on the assessed value of the property at the beginning of the calendar year. Assessed values of real property are established at the estimated current value existing in the year 1957 and of personal property at the current value at the date of the assessment.

Real property taxes are billed by the CRIM and are due in two equal installments in July and January following the assessment date. Personal property taxes are self-assessed and are due in May 15, when the property tax return is required to be filed.

The tax rate per annum is 8.08% for real property and 6.08% for personal property of which 3.83% and 1.83%, respectively, belongs to the Commonwealth of Puerto Rico and 4.25% of both percents belong to **the Municipality**. From the portion belonging to **the Municipality**, 3% represents **the Municipality’s** basic rate, which is appropriated for general purpose and, therefore, accounted for through the general fund. The remaining portion belonging to **the Municipality** of 1.25% represents the “ad-valorem” tax withheld by the CRIM as fiscal agent, and restricted for debt service, which is accounted for through the debt service fund (See note 2).

MUNICIPALITY OF PATILLAS, PUERTO RICO
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The Municipality has reached the maximum statutory tax rate limit for the basic tax while there is no limitation for the ad-valorem tax rate.

Complete real property tax exoneration is granted by the Commonwealth of Puerto Rico on the first \$15,000 of the assessed valuation of owner occupied residential units. However, **the Municipality** receives the full amount levied, except for residential units assessed at less than \$3,500, on which a complete exemption is granted. Veterans have additional exemption from taxes of \$5,000 of the assessed value of real property. The Department of Treasury instead of the property taxpayer became the source of payment in these cases.

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

The CRIM reports annually to the Municipality the estimated basic property tax and the tax to be used for the debt service, which will be collected in the fiscal year. The basic tax is advanced to **the Municipality** during such fiscal year. It is the practice to amortize these advances through the subsequent collection by the CRIM of the basic tax from the taxpayers.

The basic property tax advances from the CRIM are recorded in the general fund as other financing sources. As this tax is collected and reported by the CRIM, it is recorded in the general fund as revenue. The property tax received from the Department of Treasury, which is related to the exoneration granted by the Commonwealth of Puerto Rico is reflected as revenue in the general fund.

Since the collection of property taxes from the taxpayers is under the administration of the CRIM, the Municipality recognized as an expenditure the operational expenses allocated by the CRIM to the Municipality, which amounted to \$50,260 during 2006.

The following is a summary of the property tax advances, that resulted in an Accounts Receivable, for the year ended June 30, 2006. The resulting receivable is not presented in the general fund for Fund Financial Statement and is presented as a deferred revenue in the Government Wide Financial Statements.

Accounts Receivable:

Amortization through collections of property taxes by the CRIM	
07-01-05 – 06-30-06	\$ (5,221,003)
Advance received, 07-01-04 – 06-30-05	5,141,807
Due to Municipality - 2006	\$ (79,196)

MUNICIPALITY OF PATILLAS, PUERTO RICO
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3. DEPOSITS

The Municipality's cash and investments at June 30, 2006, were entirely covered by the Federal Depository Insurance Corporation by collateral provided by the banks and held by the Department of the Treasury pursuant to applicable laws and regulations. Cash with fiscal agent is maintained in interest-bearing accounts in the Government Development Bank for Puerto Rico and is collateralized by the Commonwealth of Puerto Rico.

Puerto Rico laws authorize governmental entities to invest in direct obligations or obligations guaranteed by the federal government or the Commonwealth of Puerto Rico. **The Municipality** is also allowed to invest in bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the federal and Commonwealth laws. During the year, **the Municipality** invested its funds in interest-bearing bank accounts, and short-term certificates of deposit if due date is not more than 90 days, the certificate considered as cash equivalents.

4. CONCENTRATION OF CREDIT RISK

The Municipality maintains its cash account in local commercial banks, whose accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000. Deposits in excess of \$100,000 are collateralized by the bank securities to property safeguard such funds. Nevertheless, Management believes that concentration of credit risk is limited because balances are deposited with high standing financial institutions.

5. MUNICIPAL LICENSE TAXES

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

The tax rates are as follow:

- 1% for financial institutions
- for all other organizations 0.5%

Taxes are payable in two equal semiannual installments on July 1 and January 1 following the levy date. If they are paid before their maturity, the taxpayer is granted certain discounts.

MUNICIPALITY OF PATILLAS, PUERTO RICO
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The deferred revenue of the general fund correspond to the business tax levied received from the next fiscal year.

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

The **Municipality** recognized an account receivable for the estimated municipal license taxes to be collected during the first two months of next year, but corresponding to current year. Municipal license taxes collected prior to June 30, but pertaining to the next fiscal year are recorded as deferred revenues.

6. INTERFUND TRANSACTIONS

Due From/To Other Funds (Fund Financial Statement)

Interfund receivables and payables generally reflect temporary loans, billings for services provided and recovery of expenditures. The balance are as follows:

Funds	Due From	Due To
General	\$ 649,592	\$ -
Head Start Program	-	-
Other funds	-	638,609
HUD Programs	-	10,983
	\$649,592	\$649,592

The inter-fund receivables and payables on Fund Financial Statement are eliminated on Statement of Net Assets (Government Wide Financial Statement).

7. INTERGOVERNMENTAL REVENUES

Sources of intergovernmental revenue consist primarily of governmental payments from the Commonwealth of Puerto Rico and in lieu of tax" payments from certain "quasipublic" corporations, such as the Puerto Rico Electric Power Authority.

Grants and subsidies received from the Commonwealth of Puerto Rico include, among others, a general subsidy for capital improvements. Almost all these intergovernmental revenues are accounted for in the general fund.

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8. DUE FROM (DUE TO) GOVERNMENTAL ENTITIES

As of June 30, 2006 balances due to governmental entities of the general fund consists of the following:

Name	Due to
Electric Puerto Rico Power Authority	\$ 232,640
Puerto Rico Retirement System	55,451
Puerto Rico Employees Association	2,956
Puerto Rico Unemployment Agency	41,864
Puerto Rico Department of Treasury	8,538
United States Treasury	9,316
Puerto Rico Telephone Co.	37,245
	\$ 388,010

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
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9. CAPITAL ASSETS

Fund Financial Statements

The Municipality charged costs of capitalizable outlays as expenditures categories in the Governmental Fund Financial Statements.

Governmental activities:	Balance 6/30/2005	Additions	Retire- ments	Balance 6/30/2006
Capital assets, not being depreciated:				
Land	\$ 272,974	\$ -	\$ (103,275)	\$ 169,699
Construction in progress	3,415,198	1,298,612	-	4,713,810
Total capital assets not being depreciated	<u>3,688,172</u>	<u>1,298,612</u>	<u>(103,275)</u>	<u>4,883,509</u>
Capital assets, being depreciated				
Buildings and building improvements	9,773,840	-	-	9,773,840
Infrastructure	-	672,125	-	672,125
Equipment	636,012	222,450	-	858,462
Vehicles	3,242,161	424,015	-	3,666,176
Total capital assets being depreciated	<u>13,652,013</u>	<u>1,318,590</u>	<u>-</u>	<u>14,970,603</u>
Less accumulated depreciation for:				
Buildings and building improvements	3,332,063	-	166,497	3,498,560
Equipment	2,684,627	-	226,530	2,911,157
Vehicles	498,077	-	39,897	537,974
Total accumulated depreciation	<u>6,514,767</u>	<u>-</u>	<u>432,924</u>	<u>6,947,691</u>
Total capital assets being depreciated, net	<u>7,137,246</u>	<u>1,318,590</u>	<u>(432,924)</u>	<u>8,022,912</u>
Governmental activities capital assets, net	<u>\$ 10,825,418</u>	<u>\$ 2,617,202</u>	<u>\$ (536,199)</u>	<u>\$ 12,906,421</u>

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

Governmental activities:	
General government	\$21,969
Public safety	28,741
Public works	336,817
Culture and recreation	39,759
Health	5,638
Total depreciation expense-governmental activities	<u>\$432,924</u>

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
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Government Wide Financial Statements

Capital assets purchased are carried at historical costs. Contributed assets are recorded at fair value as of the date donated. Additions, Improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation on capital assets is calculated using the straight-line method over the following estimated useful lives:

Vehicles, Heavy Equipment	5-25	\$300
Furniture and Fixture	5-10	\$300
Computer and Electronic Equipment	5	\$300
Buildings	50	\$1
Infrastructure	60	\$1
Improvements	20-40	\$1

In addition, the Municipality assigned a 10% residual value on most Capital Assets.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

10. CHANGES IN GENERAL LONG-TERM DEBT (continued)

General in General Long – Term Debt

The principal long-term obligation of the Municipality is obligation bonds issue to finance permanent improvements and purchases of equipment. The Municipality's long-term debt retirements are appropriated and paid from resources accumulated in the debt service fund.

The following is a summary of bonds of the Municipality of Patillas for year ended June 30, 2006.

Description	Beginning Balance	Additions	Reductions	Ending Balance
General Obligations Bonds	\$4,368,187	\$1,234,000	\$369,750	\$5,232,437

General Obligation Bonds:

Description	Original Amount	Interest Rate	Balance 06-30-06	Due Date	Due within One Year
Bonds Series 1987	\$525,000	5.0%	\$105,000	01-01-2009	\$ 33,000
Bonds Series 2004	\$200,000	2.7%-5.6%	95,000	07-01-2008	30,000
Bonds Series 2004	\$255,000	2.7%-5.0%	235,000	07-01-2026	5,000
Bonds Series 2004	\$2,740,000	2.7%-5.0%	2,535,000	07-01-2026	60,000
Bonds Series 1986	\$2,500,000	5.5% to 4.3%	105,000	07-01-2026	105,000
Bonds Series 1988	\$275,000	8.0%	3,437	07-01-2026	3,437
Bonds Series 1997	\$400,000	8.0%	280,000	07-01-2016	20,000
Bonds Series 2004	\$250,000	5.0% - 6.5%	160,000	07-01-2009	35,000
Bonds Series 2004	\$180,000	5.0% - 6.0%	135,000	07-01-2010	25,000
Bonds Series 2004	\$395,000	3.2775% to 5%	345,000	07-01-2011	50,000
Bonds Series 2005	\$259,000	4.5%	259,000	01/01/2013	\$32,000
Bond Series 2006	\$975,006	7%	975,000	7/1/2013	-0-
Total			\$5,232,437		\$398,437

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

The annual requirements to amortize all bonded debt outstanding as June 30, 2006 follows:

Year Ending	Principal	Interest	Total
2007	\$398,437	\$240,277	638,714
2008	419,000	255,437	674,437
2009	437,000	234,278	671,278
2010	397,000	107,876	504,876
2011	374,000	188,887	562,887
Subsequent years	3,207,000	1,305,558	4,512,558
Total	\$5,232,437	\$2,332,313	\$7,564,750

The Municipality is subjected to certain laws of the Commonwealth of Puerto Rico, which limit the amount of bond obligations that can be issued to 10% of the assessed valuation of the property located at the **Municipality of Patillas**.

11. DEBT SERVICE FUND

The revenues of the debt service fund arise from the additional property tax and are recognized when collected and informed by the CRIM (See Note 2). The CRIM retains these collections for the payment of principal and interest of bonds and notes issued by the Municipality. Interest income is for the payment of interest or special obligations notes and property taxes are for the debt service requirements of the genera obligations bonds and notes.

Principal and interest on these obligations are paid by the Government Development Bank for Puerto Rico from funds obtained fro the Following:

Property taxes	\$355,666
General funds	160,662
Debt service	59,721
	\$576,049

Expenditures for the year 2005-2006 were as follows:

Principal	\$369,750
Interest	206,299
	\$576,049

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

12. RETIREMENT SYSTEM

Plan Description

Regular employees of the Municipality contribute to a cost sharing multiple-employer defined benefit retirement plan, administered by the Employee Retirement System of the Government of Puerto Rico and its instrumentalities (ERS). ERS covers all regular full time public employees working for the central government, public corporations and the municipalities of Puerto Rico. The system provides retirements pensions, death and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Benefits vest after ten years of plan participation. The system was created under Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS at G.P.O. Box 42005, San Juan Puerto Rico. 00940.

The annual retirement benefits for those regular full-time employees hired on or before March 31, 1990 or those attaining permanent status before that date (Old Plan) and for those hired or attaining permanent status on or after April 1, 1990 (New Plan) are as follows:

OLD PLAN

Eligibility

Pension Benefits

Age 55 and 30 years
Of service

75% of average highest compensation
during any years of credited service

Under 55 and 30 ears
Of service

65% of average highest compensation
during any 3 years of credit service

Participant in the System who retire prior to 30 years of credited service are entitled to an annual retirement benefit equal to 1.5% of the highest compensation in any 3 years of credited service for each year of service up to 20 years, and 2% for each year in excess of 20 years.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

NEW PLAN

Eligibility

Age 65 with 10 years
of service

Pension Benefits

1.5% of average compensation during
the final 5 years of credited services
multiplied by the numbers of years
credited service

For both plans, the employees are vested when attaining ten years of credited services. Disability and death benefits are available with certain limitations and all annuities in pay status will be increased every three years by 3% subject to the approval by the Legislature of Puerto Rico.

Funding Policy

The Act 447, as amended, is the authority under which obligations to contribute to the Plan by the Plan members, employer and other contributing entities are established or may be amended. The required contributions made by **the Municipality** were based on percentages established by the Administrator of the System. Such percentages were not based on actuarial studies as required by generally accepted accounting principles. An actuarial computation of the annual contribution applicable to **the Municipality** has not been prepared. Accordingly, the amounts by which the actual contributions differ from the required actuarial contributions are not known. The Municipality's total payroll for the fiscal year 2006 amounted approximately \$4,661,218 respectively. Members' contributions are 5.775% for gross salaries up to \$6,600 plus 8.275% of the gross salary in excess, of \$6,600 the required and actual contribution \$136,612 and \$136,612 for reform 2000. The Municipality is required to contribute 9.275% of gross salary for the amount of \$150,569 and \$150,568 for the required and actual contribution.

Municipality is subject to certain laws of the Commonwealth of Puerto Rico, which limit the amount of bond obligations that can be issued to 10% of the assessed valuation of the property located at the **Municipality of Patillas**.

Actuarial Valuation

The actuarial determined present value of benefits accrued as of June 30, 2003 (latest date available) for the System as whole, determined through an actuarial valuation performed at such date, amounted to \$11.2 billion. The net assets available for benefits at such date were \$2.0 billion, resulting in an excess of accrued benefits over net assets available (actuarial deficiency) of \$9.2 billion. This information is not available by each participant government agencies or municipalities.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

Actuarial Valuation (continuation)

Net assets of the system consist principally of investments in stocks and bonds and loans to participants. The projected unit credit actuarial cost method was used for the actuarial calculation. Significant assumptions were as follows:

- | | |
|--|---|
| a) Interest rate | 8.5% a year |
| b) Salary increases | 5.0% year |
| c) Mortality | GAM'83 Mortality Table set forward two years |
| d) Termination | Medium Turnover Table commensurate with anticipated experience. |
| e) Disability | 65% of Third Railroad Retirement Table Rates. |
| f) Retirement age | Graded scale of retirement ages commensurate with anticipated experience. |
| g) Proportion of participants with spouses | 80% of participants assumed to be married, with wives assumed to be four years younger than husbands. |
| h) Number of employees electing high contributions | 15% of retiring employees assumed to pay retroactive contributions at retirement. |
| i) Cost-of-living adjustments | 3% every third year |

13. LONG TERM LIABILITIES

Compensated Absences

Account for vacation and sick leave absences to be financed with governmental funds.

The liability for compensated absences was recorded in the Government-wide financial statements. The balance consists of unpaid, accumulated annual and sick leave balances. The liability has been calculated using the vesting method. In which sick leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included.

The changes in Compensated absences for the year ended June 30, 2006 are as follows:

Governmental activity	June 30, 2005	Net Increase	June 30, 2006	Due within One year
Compensated Absences	\$695,355	\$8,836	\$704,191	\$374,645

In addition, the liabilities for retirement obligations were recorded in the Government-Wide Financial Statements. The balance consists of unpaid, accumulated pension obligations.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

14. LEASES

Operating Leases

The Municipality has several short-term operating lease agreements covering some of the Municipality's premises and equipment. Most of the agreements are renewed annually. Total rental charges for the year ended June 30, 2006, were approximately \$75,658 included in all funds.

15. CLAIMS AND CONTINGENCIES

Contingencies

As per Act No. 72 of September 7, 1993, Act of the Health Insurance of PR Administration", (HIA) should negotiate with the municipalities a contribution from the operational budget for the medical services covered by the Health Care Reform. As of June 30, 2002 the amount billed by HIA to the Municipality amounted to \$1,011,814. The Municipality alleged that the HIA never discussed the amount to be contributed by the Municipality and is determined unilaterally. The Municipality's management decided not to record the liability on the fund financial statements.

On July 1, 1997, there was an amendment to Act No. 72 in which it was established that the balance due to HIA from October 1994 to June 30, 1997 would be earned on the additional lottery games. During the year the Municipality pay to Health Insurance of PR Administration \$295,067.

Federal Programs

The Municipality participates in a number of federal financial assistance programs. Although the Municipality's grant programs have been audited in accordance with the provisions of the Single Audit Act of 1984, as amended, during the year ended June 30, 1996, these programs are still subject to financial and compliance audits and resolution of previously identified questioned costs. These grants are also subject to audit on behalf of the grantors to assure compliance with grant provisions. If expenditures are disallowed due to noncompliance with grant program requirements, the Municipality may be required to reimburse to the grantor agency. Accordingly, the Administrations compliance with applicable grant requirements will be established at some future date. Nevertheless, the Municipality's management expects the amount of expenditures, which may be disallowed by the granting agencies from such audits, to be immaterial.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2006

15. CLAIMS AND CONTINGENCIES (continued)

Comptroller's Office Audits

The Municipality of Patillas, Puerto Rico, has been audited by the Comptroller's Office of the Commonwealth of Puerto Rico. The Comptroller's Office has not issued a final report related to the financial operations of the Municipality for the period of the single audit. These audit reports do not cover any findings subsequently disclosed to Municipality operation by the Comptroller's Office.

16. SALE OF LAND

During fiscal year 2005-2006 the Municipality of Patillas sold 17 acres of a land lot comprising a total of 40 acres to a third party. Total proceeds from this sale were approximately \$405,000. The gain or sale of this land was approximately \$301,700.

17. PRIOR PERIOD ADJUSTMENTS

General Fund

Ordinance numbers 33 and 43 were approved by municipal council to increase income account of the municipality for \$339,624 by adjusting the general fund balance of prior year.

JUAN A. FELICIANO CHARNECO
Certified Public Accountant

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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 Mayor and Municipal Council
Municipality of Patillas, Puerto Rico

I have audited the accompanying financial statements of the governmental activities of the **Municipality of Patillas**, Puerto Rico, as of and for the year ended June 30, 2006, and have issued an unqualified report thereon dated November 8, 2006. I conducted my audit in accordance with generally accepted auditing standards in the United States 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 my audit, I considered **Municipality of Patillas**, Puerto Rico, internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing my opinion on the financial statements and not to provide assurance on the internal control over financial reporting. My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error of fraud in amounts that would be material in relation to the general purpose financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over financial reporting and its operation that we considered to be material weaknesses. However, I noted other matters involving the internal control over financial reporting that I have reported to management of **Municipality of Patillas**, in a separate dated November 8, 2006.

Compliance and other matters

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

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

San Juan, Puerto Rico
November 8, 2006

The stamp number
was affixed to the
original of this report

2171643

Juan A. Feliciano
CPA JUAN A. FELICIANO CHARNICO
License No. 1263
Expires December 1, 2007



JUAN A. FELICIANO CHARNECO
Certified Public Accountant

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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 Mayor and Municipal Council of the Municipality of Patillas
Patillas, Puerto Rico

Compliance

I have audited the compliance of the **Municipality of Patillas**, Puerto Rico, 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 Patillas** major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Municipality of Patillas Management. My responsibility is to express an opinion on **Municipality of Patillas** compliance based on my audit.

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

In my opinion, the **Municipality of Patillas**, 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 my auditing procedures disclosed instances of noncompliance with those requirements that 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 2006-01, 2006-02 and 2006-03 and 2006-04.

Internal Control Over Compliance

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

My consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a 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 the 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. I noted no matters involving the internal control over compliance and its operation that I consider being material weaknesses.

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

San Juan, Puerto Rico
November 8, 2006

The stamp number
was affixed to the
original of this report

2171644

Juan A. Feliciano
CPA JUAN A. FELICIANO CHARNECO
License No. 1263
Expires December 1, 2007



MUNICIPALITY OF PATILLAS, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006

Federal Grantor / Pass-through Grantor Program Title	Federal CFDA Number	Pass-through Grantors Number	Federal Expenditures
<u>U.S. Department of Housing and Urban Development</u>			
Direct Program:			
Department of Housing and Urban Development Public and Indian Housing			
Section 8 - Voucher	14-871	RQ46-EO-57-001/002	\$ 345,585
			<u>345,585</u>
Passed-through Commonwealth of Puerto Rico	14-228	AC-2005	6,404
Commissioners Office of Municipal Affairs	14-228	FC-2005	242,387
	14-228	DR-2005	415
	14-228	AB-2004	263,538
	14-228	FC-2004	116,919
	14-228	AB-2003	91,919
	14-228	FC-2003	64,237
	14-228	FE-2003	1,000
	14-228	AB-2002	29,992
Community Planning and Development	14-228	FC-2002	15,561
Community Development Block Grant (State Program)	14-228	2001	904
	14-228	2000	5,068
	14-228	1999	55,324
	14-228	1998	61,746
	14-228	1998	4,827
	14-228	1997	75,371
	14-228	1996	1,563
	14-228	1993	4,117
			<u>1,041,292</u>
			<u>1,386,877</u>
U.S. Department of Health and Human Services:			
Passed-through Governors Office for Human Development:			
Administration for Children and Families			
Child Care	93-575	-	89,672
Head Start	93-600	-	784,290
Red de Cuido	n/a	-	43,419
Even Start	n/a	-	7
			<u>917,388</u>
<u>U.S. Federal Emergency Management Agency:</u>			
Passed-through Emergency Management State and Local Assistance			
FEMA (Lluvia noviembre)	83-534	1247	13,881
FEMA (Tormenta Jeanne)	83-534	1552	105,472
			<u>119,353</u>
<u>U.S. Department of Agriculture</u>			
Passed-through Commonwealth of Puerto Rico, Department of Education			
Child Care Food Program (USDA)	10-558		5,643
Head Start Food Program			51,149
			<u>56,792</u>
			<u>\$ 2,480,410</u>

See notes to the schedule of expenditures of federal awards.

**MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO THE SCHEDULE
OF EXPENDITURES OF FEDERAL FINANCIAL AWARDS
FOR THE FISCAL YEAR THEN ENDED JUNE 30, 2006**

(1) GENERAL

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Municipality of Patillas, Puerto Rico and is presented on the modified accrual basis of accounting. The reporting entity is defined in Note 1 to the financial statements of the Municipality. 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) MAJOR FEDERAL AWARDS

The Community Development Block grants, Housing Assistance Payments Programs and Health and Human Services Programs represent the major federal financial awards of the Municipality. Major federal awards represent 88% of total expenditures.

(3) FEDERAL CFDA NUMBER

The CFDA numbers included in this schedule were determined based on the program name review of grant contract information and the office of management and budget catalog of Federal Domestic Assistance.

(4) RELATIONSHIP TO GENERAL PURPOSE FINANCIAL STATEMENTS

Federal financial assistance expenditures are reported in the Municipality of Patillas, Puerto Rico Combined Statement of Revenues, Expenditures and Change in Fund Balances All Governmental and Types as follow:

Description	HUD Programs	Head Start Programs	Other funds	Total
Federal Programs Expenditures	\$1,386,877	\$917,381	\$176,152	\$2,480,410
State & Municipal Expenditures	-	-	515,414	515,414
Total Expenditures	\$1,386,877	\$917,381	\$691,566	\$2,995,824

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006**

A. Summary of Audit results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness (es) identified? Yes No

Reportable condition(s) identified not considered
to be material weaknesses? Yes No
None reported

Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

Material weakness(es) identified? Yes No

Reportable condition(s) identified not
Considered being material weaknesses? Yes No

Type of auditor's report issued on compliance considered
for major programs Unqualified

Any audit findings disclosed that are required to be
Reported in accordance with Circular A-133,
Section .510(a) are reported Yes No

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006**

Identification of Major Programs

CFDA Number(s)	Name of Federal Program or Cluster
14.871	Section 8 – Voucher
93.600	Head Start
14.228	CDBG

Dollar threshold used to distinguish
Between type A and type B Programs 300,000

Auditee qualified as low-risk audit X Yes No

B - Financial Statements Findings

No matters were reported regarding reportable conditions, material weaknesses, and instances of non-compliance related to the financial statements that are required to be reported in accordance with paragraph 5.18 through 5.20 of Governmental Auditing Standards.

C – Federal Award Findings and Questioned Cost

**U.S. Department of Housing and Urban Development
Passed-through Governor’s Office (OCAM)
CFDA No. 14-228
Grant No. Community Development
Block Grant (State Program) CDBG
Year ended June 30, 2006**

Ref. No. Finding / Noncompliance

2006-01 Statement of Condition and Criteria

It was noted in my test of compliance that the Municipality’s financial management system is not complying with the cash management requirements established by the United States Treasury. According to these requirements the Municipality had to establish procedures to minimize the time elapsing between the transfer of funds from the Office of the Administration for Children and Families and the disbursements by the Municipality. It was noted during my audit that Municipality held cash balances over \$5,000 for periods longer than 3 days.

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006
(continued)

Cause

The Municipality did not comply with the Cash Management Requirements of the Department of Treasury of the United States.

Effect

The Municipality did not maintain adequate procedures for the Administration of cash to determine properly their use needs.

Auditor's Recommendation

The Municipality should establish adequate procedures in order to control in a more effective manner the need and use of the federal funds.

Municipality Response:

We concur with auditor's recommendations. The Municipality evaluates the actual administrative procedures followed to establish a procedure to minimize the time between the funds received and the disbursements.

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006
(continued)

U.S. Department of Agriculture
Head Start Food Program
Passed-through Department of Education
CFDA No. 10-558
Grant No. None identified
Year ended June 30, 2006

Ref. No.	Finding / Noncompliance
-----	-----
2006-02	<u>Statement of Condition and Criteria</u>

It was noted in my test of compliance that the Municipality's financial management system is not complying with the cash management requirements established by the United States Treasury. According to these requirements the Municipality had to establish procedures to minimize the time elapsing between the transfer of funds from the Office of the Department of Agriculture and the disbursements by the Municipality. It was noted during my audit that Municipality held cash balances over \$5,000 for periods longer than 3 days.

Cause

The Municipality did not comply with the Cash Management Requirements of the Department of Treasury of the United States.

Effect

The Municipality did not maintain adequate procedures for the Administration of cash to determine properly their use needs.

Auditor's Recommendation

The Municipality should establish adequate procedures in order to control in a more effective manner the need and use of the federal funds.

Municipality Response:

We concur with auditor's recommendations. The Municipality evaluates the actual administrative procedures followed to establish a procedure to minimize the time between the funds received and the disbursements.

**MUNICIPALITY OF PATILLAS
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 YEAR ENDED JUNE 30, 2006
 (continued)**

**Department of Housing and Urban Development
 Public and Indian Housing
 CFDA No. 14-871
 Grant No. Section 8 - Voucher
 Year ended June 30, 2006**

Ref. No.	Finding / Noncompliance	Questioned Cost
-----	-----	-----
2006-03	<p><u>Statement of Condition and Criteria</u> It was noted in my test of compliance that the Municipality is not complying with the criteria established by the Standards of Financial management Systems, Sub-part C, Section 21, b., 24 CFR, Section 982.158 Uniform Administrative Requirements.</p> <ol style="list-style-type: none"> 1. Accurate, current and complete disclosure of the financial results of federally sponsored projects of programs. 2. Records that identify adequately the source and application of funds. The records shall contain information pertaining to federal awards, authorization, obligations, un-obligated balances, assets, outlays, income and interest. 3. Effective controls and accountability for funds, property and other assets. <p>To establish procedures to comply with Financial and Program Management Standards of funds of the Section 8 Voucher Program. It was noted during my audit that the Municipality modify the proper accounting records to comply standard require.</p> <p><u>Cause</u> The Municipality did not comply with the Financial and Program Management System Standards.</p>	<p>-0-</p> <p style="font-size: 2em; vertical-align: middle;">N/A</p>

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006
(continued)

Effect

The Municipality did not maintain adequate procedures for the Administration of funds from Section 8 Voucher Program.

Auditors Recommendation

The Municipality must establish adequate procedures in order to comply in a more effective manner with the Financial and Program Management System Standards

Municipality Response:

We concur with auditor's recommendations. The Municipality will correct the accounting system before June 30, 2007 and before the audit was is completed.

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006
(continued)

U.S. Department of Housing and Urban Development
Public and Indian Housing
CFDA No. 14-871
Grant No. Section 8 Voucher
Year ended June 30, 2006

Ref. No.	Finding / Noncompliance
-----	-----
2006-04	<u>Statement of Condition and Criteria</u>

It was noted in my test of compliance that the Municipality's financial management system is not complying with the cash management requirements established by the United States Treasury. According to these requirements the Municipality had to establish procedures to minimize the time elapsing between the transfer of funds from the Office of the Department of Housing and Urban Development Public and Indian Housing and the disbursements by the Municipality. It was noted during my audit that Municipality held cash balances over \$5,000 for periods longer than 3 days.

Cause

The Municipality did not comply with the Cash Management Requirements of the Department of Treasury of the United States.

Effect

The Municipality did not maintain adequate procedures for the Administration of cash to determine properly their use needs.

Auditor's Recommendation

The Municipality should establish adequate procedures in order to control in a more effective manner the need and use of the federal funds.

Municipality Response:

We concur with auditor's recommendations. The Municipality evaluates the actual administrative procedures followed to establish a procedure to minimize the time between the funds received and the disbursements.

MUNICIPALITY OF PATILLAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2006

2005 – Finding No. 1: U.S. Department of Health and Human Services
Passed-through Office of Children and Families Administration
CFDA No. 93-600
Grant No. 02-CH-0483/03
Year ended June 30, 2005
Finding was corrected

2005 – Finding No. 2: U.S. Department of Agriculture
Child Care Food Program
Passed-through Department of Education
CFDA No. 10-558
Grant No. None identified
Year ended June 30, 2005
Finding was corrected

2005 – Finding No. 3: U.S. Department of Housing and Urban Development
Passed-through 14-228-558
Grant No. Community Development
Block Grant (State Program) SBGP
Year ended June 30, 2005
Finding was corrected



GOBIERNO MUNICIPAL DE PATILLAS
OFICINA DEL ALCALDE
APARTADO 698
PATILLAS, PUERTO RICO



CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2006
(continued)

Ref. No.	<u>Finding /Corrective Action Planned/Person Responsible:</u>	<u>Anticipated Completion Date</u>
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Statement of Condition:

The CDBG Program cash balance over \$5,000 for the periods end longer 3 days.

On or before

end of 2006-07
Fiscal year

Corrective Action Planned:

The Municipalities Administration will evaluate and implement adequate procedures to control and use in a effective manner federal funds. Standards for financial management system.

Person Responsible:

Mr. Narciso Velázquez Rodríguez, Finance Director

Ref. No.	<u>Finding /Corrective Action Planned/Person Responsible:</u>	<u>Anticipated Completion Date</u>
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Statement of Condition:

The Head Start Food Program cash balance over \$5,000 for periods longer than 3 days

On or before

end of 2006-07
fiscal year

Corrective Action Planned:

The Head Start Food Program Administrator will establish adequate procedures to control and use in an effective manner, federal funds.

Person Responsible:

Mr. Narciso Velázquez Rodríguez, Finance Director

**CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2006
(continued)**

Ref. No.	<u>Finding /Corrective Action Planned/Person Responsible:</u>	<u>Anticipated Completion Date</u>
2006-03	<p><u>Statement of Condition:</u> The Section 8 voucher program cash balance over \$5,000 for the periods larger than 3 days.</p> <p><u>Corrective Action Planned:</u> The Section 8 voucher program Administration will evaluate and implement adequate procedures to control and use in effective manner, federal funds.</p> <p><u>Person Responsible:</u> Mr. Narciso Velázquez Rodríguez, Finance Director</p>	<p>On or before end of 2006-07 Fiscal year</p>
2006-04	<p><u>Statement of Condition:</u> The Section 8 voucher Program Management System Standards.</p> <p><u>Corrective Action Planned:</u> The CDBG Program Administrator Established adequate and correct the finding before the audit report was issued.</p> <p><u>Person Responsible:</u> Mr. Narciso Velázquez Rodríguez, Finance Director</p>	<p><u>Anticipated Completion Date</u></p> <p>On or before end of 2006-07 fiscal year</p>