OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES

AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE PATILLAS
AUDITORIA 2006-2007

30 DE JUNIO DE 2007

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MUNICIPALITY OF PATILLAS, PUERTO RICO
SINGLE AUDIT REPORT
JUNE 30, 2007
(INDEPENDENT AUDITOR'S REPORT)

*Juan Feliciano Charneco * Certified Public Accountant*

MUNICIPALITY OF PATILLAS, PUERTO RICO
SINGLE AUDIT REPORT
JUNE 30, 2007

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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, 2007. We encourage readers to consider the information presented here in conjunction with the Municipality's financial statements.

Fiscal year 2006-2007 operations sustain the Municipality's track of solvency and sound fiscal condition. The Governmental Wide financial statements 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 $12,473,937 (net assets).
- The adjusted actual of the General Fund operations resulted in a favorable variance of $9,595 as compared to the revised budget.
- As June 30, 2007 the Municipality's General Fund (the primary operating fund) reported a fund balance of $67,662 a decrease of $236,749 in comparison with the prior year.
- Loans principal payments were $400,000 during fiscal year 2006-07. Loan proceeds from new debt issued amounted to $510,000 during the same fiscal year.
- During fiscal year 2006-2007 the General Fund received an increase of approximately $1,066,000, related with construction permits, licenses and fees.

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.

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. All 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.

The Statement of Net Assets and the statement of activities, on page 10-11, report the Municipality net assets and changes in them. One can analyze of the Municipality's net assets, as the difference between assets and liabilities, as one way to measure the Municipality's financial position. Over time increase decreases in the Municipality's net assets are one indicator of whether its financial health is improving or deteriorating. However, other non-financial factors should be considered, such as changes in the Municipality's property tax base, and the condition of roads, to assess the overall health of the Municipality's of Patillas.

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, on pages 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 spent 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.

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 valuated and reported within the Governmental column of the Governmental Wide Statement. Additionally, the government must elect to either depreciate these assets over theirs 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.

Government-Wide and fund financial Statements

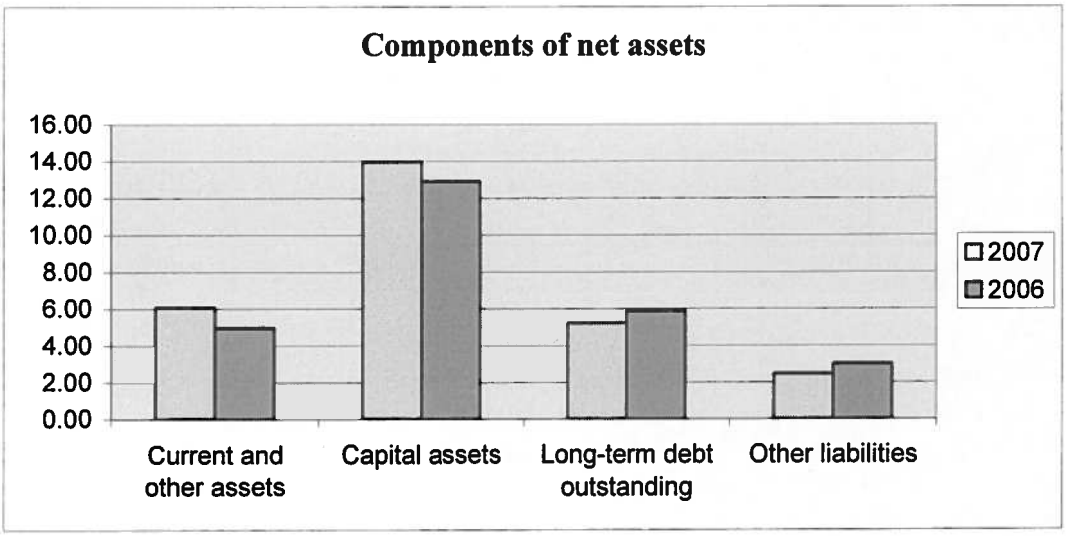
Statement of Net Assets

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 $12,473,937 at the close of the recent fiscal year. The following reflects the condensed Statement of Net Assets of the Primary Government.

Statements of Net Assets
As of June 30, 2007 and 2006

	2007	2006
Current and other assets	$ 6,057,354	$ 4,948,127
Capital assets	13,971,230	12,906,421
Total assets	**20,028,584**	**17,854,548**
Current and other liabilities	2,444,681	3,000,553
Long-term liabilities	5,109,966	5,880,293
Total liabilities	**7,554,647**	**8,880,846**
Net assets:		
Invested in capital assets, net of related debt	9,602,230	8,648,984
Debt service	874,270	956,599
Special and other funds	132,590	363,265
Capital project fund	3,341,796	1,250,053
Unrestricted (deficit)	(1,476,949)	(2,245,199)
Total net assets	**$ 12,473,937**	**$ 8,973,702**

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.



MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS

Statements of Activities

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

For the years ended June 30, 2007 and 2006

	2007	2006
General Revenue	$ 10,909,771	$ 9,057,875
Program Revenue	2,078,197	3,288,375
Total Revenue	**12,987,968**	**12,346,250**
Expenses		
Governmental activities	(10,994,033)	(10,912,644)
Changes in net assets	**$ 1,993,935**	**$ 1,433,606**

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

Governmental Funds
Balance Sheets
June 30, 2007 and 2006

	2007	2006
Assets:		
Cash	$ 4,444,725	$ 1,599,031
Restricted Cash	874,270	2,997,368
Accounts Receivable	3,324,897	1,930,765
Total Assets	**$ 8,643,892**	**$ 6,527,164**
Liabilities and Fund Balance		
Liabilities:		
Total Liabilities	**$ 4,227,574**	**$ 3,157,441**
	-	
Funds Balances	4,416,318	3,369,723
Total liabilities and Fund Balances	**$ 8,643,892**	**$ 6,527,164**

The most significant changes in this statement were as follows:

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

Statement or Revenues, Expenditures and Changes in Fund Balances
Years Ended June 30, 2007 and 2006

	2007	2006
Revenues:		
Property taxes	$ 1,663,936	$ 1,487,869
Volume of business tax	643,302	531,386
Intergovernmental revenue	7,188,945	5,323,831
Federal grants	2,077,967	2,697,496
Other	1,566,589	830,471
Total Revenues	**$ 13,140,739**	**$ 10,871,053**
Liabilities and Fund Balance		
Expenditures:		
General Government	$ 4,092,845	$ 3,752,664
Public safety and public work	3,443,860	2,408,473
Education and training and culture	1,693,031	1,539,457
Capital projects	1,413,162	1,193,139
Other	525,864	1,379,688
Bonds, notes and interest	666,102	576,049
Total Expenditures	**$ 11,834,864**	**$ 10,849,470**
Excess of revenues (expenditures)		
Over expenditures (revenues)	**$ 1,305,875**	**$ 21,583**

The most significant changes of this statement were as follows:

- The larger increases in revenues are related to intergovernmental revenues for the amount of $1,865,114 and to other revenues for the amount of $736,118.
- The most significant change in the expenditures were an increase in public safety and public works for approximately one million and increase in capital projects for approximately $1.4 millions related with capital outlays.

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 2006-2007 is $1,539,151 more than the last fiscal year (2005-2006).

Contacting the Municipality's Financial Management

The Municipality's financial statements are designed to present users with general overview of the Municipality's finances and to show the accountability for the money it receives. If you have questions about the report, or need additional financial information, contact us at the Municipality of Patillas, PO Box 698, Patillas, Puerto Rico 00723.

Narciso Velázquez Rodríguez
Finance Director

JUAN A. FELICIANO CHARNECO
Certified Public Accountant

Urbanización Matienzo
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Tel: (787) 879-4433
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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, 2007, 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, 2007, 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 October 31, 2007 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.

Arecibo, Puerto Rico
October 31, 2007

CPA JUAN A. FELICIANO CHARNECO
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MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF NET ASSETS
JUNE 30, 2007

ASSETS	Governmental Activities
Cash and investments	$ 4,444,725
Cash with fiscal agent and other	874,270
Account receivable (volume business)	95,731
Accounts receivable other	170,731
Accounts receivable federal government	354,105
Accounts receivable government	117,792
Capital assets	13,971,230
Total assets	**$ 20,028,584**
LIABILITIES AND FUND EQUITY	
Liabilities:	
Accounts payable and accrued liabilities	$ 936,184
Due to government entity	283,736
Deferred revenue	420,878
Noncurrent liabilities:	
Due within one year	803,883
Due in more than one year	5,109,966
Total liabilities	**7,554,647**
NET ASSETS	
Invested in capital assets, net of related debt	9,602,230
Restricted for:	
Debt service	874,270
Special and other fund	132,590
Capital project fund	3,341,796
Unrestricted (Deficit)	(1,476,949)
Total net assets	**12,473,937**
Total Liabilities and net Assets	**$ 20,028,584**

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

Functions/Programs	Expenses	Program Revenues: Charges for Services	Program Revenues: Capital Grants and Contributions	Program Revenues: Operating Grants and Contributions	Net (expense) revenue and change in Net Assets Governmental Activities
EXPENDITURES:					
General government	$ 4,118,957	$ (230)	$ (676,847)	$ (98,184)	$ 3,343,696
Public safety	597,664	-	-	-	597,664
Public works	3,280,803	-	-	-	3,280,803
Capital projects	466,702	-	(466,702)	-	-
Health	531,502	-	-	-	531,502
Culture and recreation	896,069	-	-	-	896,069
Education and training	836,234	-	-	(836,234)	-
Interest on long -term debt	266,102	-	-	-	266,102
Total governmental activities	**$ 10,994,033**	**$ (230)**	**$ (1,143,549)**	**$ (934,418)**	**8,915,836**
GENERAL REVENUES:					
Property taxes					1,546,217
Municipal licenses tax					643,302
Licenses, permits and fines					1,393,517
Intergovernmental revenues					7,188,945
Rent of properties					109,641
Interest revenues					2,980
Other revenues					25,169
Total general revenues					**10,909,771**
Changes in net assets					1,993,935
Net assets at beginning of year					8,973,702
Prior period adjustment					1,506,300
Net assets at end of year					**$ 12,473,937**

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2007

ASSETS	General Fund	2006 and 2007 Bonds Issue Fund	HUD Programs	Head Start Programs	Debt Service Fund	Other Funds	Total Governmental Funds
Cash and investments	$ 1,797,888	$ 1,908,493	$ 118,530	$ 7,362	$ -	$ 612,452	$ 4,444,725
Cash with fiscal agent and other	-	-	-	-	874,270	-	874,270
Account receivable (volume business)	95,731	-	-	-	-	-	95,731
Accounts receivable other	170,493	-	-	-	-	-	170,493
Accounts receivable federal government	-	-	117,137	116,227	-	120,741	354,105
Accounts receivable government	117,792	-	-	-	-	-	117,792
Due from other funds	921,623	-	-	-	-	1,665,153	2,586,776
Total assets and other debits	$ 3,103,527	$ 1,908,493	$ 235,667	$ 123,589	$ 874,270	$ 2,398,346	$ 8,643,892
LIABILITIES AND FUND BALANCES							
Liabilities:							
Accounts payable and accrued liabilities	$ 666,098	$ -	$ 56,558	$ 83,283	$ -	$ 130,245	$ 936,184
Due to special revenue funds	1,665,153	-	-	-	-	-	1,665,153
Due to general fund	-	-	22,617	16,276	-	882,730	921,623
Due to government entities	283,736	-	-	-	-	-	283,736
Deferred revenue	420,878	-	-	-	-	-	420,878
Total liabilities	3,035,865	-	79,175	99,559	-	1,012,975	4,227,574
Fund balances:							
Reserve for debt services	-	-	-	-	874,270	-	874,270
Encumbrances	23,000	-	-	-	-	-	23,000
General Fund	44,662	-	-	-	-	-	44,662
Special and other funds	-	-	56,123	24,030	-	52,437	132,590
Capital project fund	-	1,908,493	100,369	-	-	1,332,934	3,341,796
Total fund balances	67,662	1,908,493	156,492	24,030	874,270	1,385,371	4,416,318
Total liabilities and fund balance	$ 3,103,527	$ 1,908,493	$ 235,667	$ 123,589	$ 874,270	$ 2,398,346	$ 8,643,892

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET NET ASSETS:

TOTAL FUND BALANCE - GOVERNMENTAL FUNDS		$ 4,416,318
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		13,971,230
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 absences	$ 679,611	
Bonds payable	5,234,000	
	$ 5,913,611	(5,913,611)
TOTAL NET ASSETS OF GOVERNMENTAL ACTIVITIES		$ 12,473,937

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, 2007

	General Fund	2007 Bonds issue Fund	HUD Programs	Head Start Program	Debt Service Fund	Other Funds	Total Governmental Funds
REVENUES:							
Property taxes	$ 1,299,480	$ -	$ -	$ -	$ 364,456	$ -	$ 1,663,936
Municipal license tax	643,302	-	-	-	-	-	643,302
Licenses, permits and fines	1,393,747	-	-	-	-	-	1,393,747
Intergovernmental revenues	4,805,127	-	-	-	-	2,383,818	7,188,945
Rent of properties	74,680	-	-	-	34,961	-	109,641
Interest income	38,032	-	-	-	-	-	38,032
Other revenues	25,169	-	-	-	-	-	25,169
Federal financial award	-	-	1,143,549	864,784	-	69,634	2,077,967
Total revenues	**8,279,537**	**-**	**1,143,549**	**864,784**	**399,417**	**2,453,452**	**13,140,739**
EXPENDITURES:							
Current:							
General government	2,983,261	-	688,400		-	421,184	4,092,845
Public safety	574,280	-	-	-	-	-	574,280
Public works	2,869,580	-	-	-	-	-	2,869,580
Health	525,864	-	-	-	-	-	525,864
Capital projects	-	-	466,702	-	-	946,460	1,413,162
Culture and recreation	856,797	-	-	-	-	-	856,797
Education and training	-	-	-	836,234	-	-	836,234
Debt service:							
Principal retirement	-	-	-	-	400,000	-	400,000
Interest and fiscal charges	-	-	-	-	266,102	-	266,102
Total expenditures	**7,809,782**	**-**	**1,155,102**	**836,234**	**666,102**	**1,367,644**	**11,834,864**
Excess of revenues over (under) expenditures	469,755	-	(11,553)	28,550	(266,685)	1,085,808	1,305,875
OTHER FINANCING SOURCES (USES):							
Transfer in (out) to debt service fund	(219,408)	-	-	-	219,408	-	-
interest expenditure	-	-	-	-	(35,052)	-	(35,052)
Net bond issued debt	-	500,000	-	-	-	-	500,000
Bond Expenditure	-	(157,276)	-	-	-	-	(157,276)
Total other financing sources (uses)	(219,408)	342,724	-	-	184,356	-	307,672
Excess of revenues over (under) expenditures and other uses and other sources	250,347	342,724	(11,553)	28,550	(82,329)	1,085,808	1,613,547
Fund balance June 30, 2006	304,411	1,565,769	179,679	-	956,599	363,265	3,369,723
Prior period adjustment (Note 17)	(487,096)	-	(11,634)	(4,520)	-	(63,702)	(566,952)
Fund balance June 30, 2007	**$ 67,662**	**$ 1,908,493**	**$ 156,492**	**$ 24,030**	**$ 874,270**	**$ 1,385,371**	**$ 4,416,318**

See notes to financial statements.

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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, 2007

Amounts reported for governmental activities in the statement of activities are different because:		
Net change in fund balance - total governmental funds		**$ 1,305,875**
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	946,460	
Less: current year depreciation	(505,629)	
		440,831
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	(500,000)	
Principal payments	400,000	
Bond expenditure	157,276	
		57,276
Some expenses reported in the statement of activities de not require the use of current financial resources and, therefore, are not reproted as expenditures in governmental funds.		189,953
Change in net assets of governmental activities		**$ 1,993,935**

See notes to financial statements.

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, 2007

	Budgeted Amounts Original	Budgeted Amounts Final	Adjusted Actual Note 1	Variance Favorable (Unfavorable)
REVENUES:				
Property taxes	$ 298,686	$ 298,686	$ 298,686	$ -
Municipal license tax	502,000	643,257	643,302	45
Intergovernmental revenues	4,778,135	4,942,344	4,805,127	(137,217)
Licenses, permits and fines	151,500	1,248,559	1,393,747	145,188
Rent of properties	100,000	100,000	74,680	(25,320)
Interest income	11,500	42,149	38,032	(4,117)
Other revenues	125,500	1,156,797	25,169	(1,131,628)
Other sources	883,075	883,075	883,075	-
Property tax (debt service)	410,354	316,180	399,417	83,237
Total revenues	**$ 7,260,750**	**$ 9,631,047**	**$ 8,561,235**	**$ (1,069,812)**
EXPENDITURES:				
Current:				
General government	$ 2,365,671	$ 4,425,211	$ 3,063,355	$ 1,361,856
Public safety	739,017	575,941	574,280	1,661
Public Work	2,750,599	2,882,203	2,869,580	12,623
Health	435,040	525,966	525,863	103
Culture and recreation	522,844	868,320	856,797	11,523
Transfer to debt service	37,225	37,225	219,408	(182,183)
Principal and interest	410,354	316,180	442,357	(126,177)
Total expenditures	**$ 7,260,750**	**$ 9,631,047**	$ 8,551,640	$ 1,079,407
Excess of revenues over (under) expenditures			**$ 9,595**	**$ 9,595**

Explanation of differences:

Sources/inflows of resources:	
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule	$ 8,561,235
Differences - budget to GAAP:	
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes.	117,719
Total revenues as reported on the statement of revenue, expenditure, and changes in fund balances	**$ 8,678,954**
Uses/outflow of resources	
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	$ 8,551,640
Differences - budget to GAAP:	
Non budgeted expenditures	283,736
Budgeted expenditures included prior year	(359,492)
Total expenditures as reported on the statement of revenue, expenditures and change in fund balances	**$ 8,475,884**

See notes to budgetary comparison schedule.

See notes to financial statements.

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.

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 the 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, 2007 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 in 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.

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.

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 90 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.

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 an 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:

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 $2,370,297 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.

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.

Governm ent 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.

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.

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.

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 ad 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).

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 $44,937 during 2007.

The following is a summary of the property tax advances, that resulted in an Accounts Receivable, for the year ended June 30, 2007. The resulting receivable is presented in the general fund for Fund Financial Statement and is presented as revenue in the Government Wide Financial Statements.

Accounts Receivable:

Amortization through collections of property taxes by the CRIM	
07-01-06 - 06-30-07	$ (5,392,367)
Advance received, 07-01-06 - 06-30-07	5,274,648
Due to Municipality - 2007	**$ (117,719)**

3. DEPOSITS

The Municipality's cash and investments at June 30, 2007, 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 collaterized 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 collaterized 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.

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	$ 921,623	$ -
Head Start Programs	-	16,276
Other funds		882,730
HUD Programs	-	22,617
	$ 921,623	**$ 921,623**

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.

8. DUE TO GOVERNMENTAL ENTITIES

As of June 30, 2007 balances due to governmental entities of the general fund consists of the following:

Name	Due to
Puerto Rico Retirement System	$ 88,487
Puerto Rico Employees Association	4,257
Puerto Rico Water System	176,955
Administration of General Services	14,037
	$ 283,736

9. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2007 was as follows:

Governmental activities:	Balance 6/30/2006	Additions	Retire-ments	Balance 6/30/2007
Capital assets, not being depreciated:				
Land	$ 169,699	$ 22,500	$ -	$ 192,199
Construction in progress	4,713,810	416,522	-	5,130,332
Total capital assets not being depreciated	4,883,509	439,022	-	5,322,531
Capital asets, being depreciated				
Buildings and building improvements	9,773,840	-	-	9,773,840
Infraestructure	672,125	1,116,265	-	1,788,390
Equipment	858,462	15,151	-	873,613
Vehicles	3,666,176	-	-	3,666,176
Total capital assets being depreciated	14,970,603	1,131,416	-	16,102,019
Less accumulated depreciation for:				
Buildings and building improvements	3,498,560	-	177,153	3,675,713
Infraestructure	-	-	181,109	181,109
Equipment	2,911,157	-	137,285	3,048,442
Vehicles	537,974	-	10,082	548,056
Total accumulated depreciation	6,947,691	-	505,629	7,453,320
Total capital assets being depreciated, net	8,022,912	1,131,416	(505,629)	8,648,699
Governmental activities capital assets, net	**$ 12,906,421**	**$ 1,570,438**	**$ (505,629)**	**$ 13,971,230**

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

Governmental activities:	
General government	$ 26,112
Public safety	23,384
Public works	411,223
Culture and recreation	39,272
Health	5,638
Total depreciation expense governmental activities	**$ 505,629**

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.

Fund Financial Statements

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

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, 2007.

Description	Beginning Balance	Additions	Reductions	Ending Balance
General Obligations Bonds	$5,124,000	$510,000	$400,000	$5,234,000

General Obligation Bonds:

Description	Original Amount	Interest Rate	Balance 06-30-07	Due Date	Due within One Year
Bonds Series 1987	$ 525,000	5.0%	$ 72,000	1/1/2009	$ 35,000
Bonds Series 2004	200,000	2.7%-5.6%	65,000	7/1/2008	30,000
Bonds Series 2004	255,000	2.7%-5.0%	230,000	7/1/2026	5,000
Bonds Series 2004	2,740,000	2.7%-5.0%	2,475,000	7/1/2026	65,000
Bonds Series 1997	400,000	8.0%	260,000	7/1/2016	20,000
Bonds Series 2004	250,000	5.0%-6.5%	125,000	7/1/2009	40,000
Bonds Series 2004	180,000	5.0%-6.0%	110,000	7/1/2010	25,000
Bonds Series 2004	395,000	3.2775% to 5%	295,000	7/1/2011	55,000
Bonds Series 2005	259,000	4.5%	227,000	1/1/2013	34,000
Bonds Series 2006	975,000	7%	865,000	7/1/2013	110,000
Bond Series 2007	410,000	6.48% - 7.5%	410,000	7/1/2031	5,000
Bond Series 2008	100,000	6.48% - 7.5%	100,000	7/1/2031	5,000
TOTAL	**6,689,000**		**$ 5,234,000**		**$ 429,000**

The annual requirements to amortize all bonded debt outstanding as June 30, 2007 follows:

Year Ending	Principal	Interest	Total
2008	429,000	272,789	701,789
2009	447,000	271,188	718,188
2010	407,000	243,041	650,041
2011	384,000	224,512	608,512
2012	385,000	200,493	585,493
Subsequent years	3,182,000	1,526,461	4,708,461
	$ 5,234,000	**$ 2,738,484**	**$ 7,972,484**

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 from the Following:

Property taxes	$ 399,417
General funds	219,408
Prior year debt service fund	47,277
	$ 666,102

Expenditures for the year 2006-2007 were as follows:

Principal	$ 400,000
Interest	266,102
	$ 666,102

12. RETIREMENT SYST EM

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 retirement pensions, death and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members 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 years 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.

NEW PLAN

Eligibility	Pension Benefits
Age 65 with 10 years of service	1.5% of average compensation during the final 5 years of credited services multiples 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 2007 amounted to approximately $4,930,394. Members' required contributions are 5.775% of gross salaries up to $6,600 plus 8.275% of the gross salary in excess of $6,600. The Municipality is required to contribute 9.275% of gross salary annually during year 2007, the Municipality's required and actual contribution under Act 447 and Reforma 2000 were $146,426 and $144,567 respectively.

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, 2005 (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.

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, 2007 are as follows:

Governmental activity	June 30, 2006	Net Decrease	June 30, 2007	Due within One year
Compensated Absences	**$ 704,191**	**$ 24,580**	**$ 679,611**	**$ 374,645**

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, 2007, were approximately $80,737 included in all funds.

15. CLAIMS AND CONTINGENCIES

Contingencies

As pr 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, 2007 the amount billed by HIA to the Municipality amounted to $608,916. 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, 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 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.

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 a period before the single audit. These audit reports do not cover any findings subsequently disclosed to Municipality operation by the Comptroller's Office.

16. SUBSEQUENT EVENT

Law of Number 117 of July 4, 2006, as amended, that was approved to establish a sales tax of 1.5% over retail sales in the municipality will be effective commencing on August, 2007. The monies collected through the above mentioned sales tax will be used, among other purposes for the management for improvements in the Municipality's infrastructure.

17. PRIOR PERIOD ADJUSTMENTS

General Fund

Ordinance numbers 42, 49 and 62 were approved by municipal council to increase income account of the municipality for $487,096 by adjusting the general fund balance of prior year.

JUAN A. FELICIANO CHARNECO
Certified Public Accountant

Urbanización Matienzo
151 Calle Miguel Salas
Arecibo, PR 00612

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Fax: (787) 880-1402

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 STANDARS

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

I have audited the financial statements of the governmental activities of Municipality of Patillas, Puerto Rico as of and for the year ended June 30, 2007 and have issued my report thereon dated October 31, 2007. I 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.

Internal Control Over Financial Reporting

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

My consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, I identified certain deficiencies in internal control over financial reporting that I consider to be significant deficiencies.

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

the of the Municipality of Patillas, Puerto Rico's financial statements that is more than inconsequential will not be prevented or detected by the Municipality of Patillas, Puerto Rico's internal control. I consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting 2007-1, 2007-3 and 2007-04.

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

My consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies or material weaknesses. I did not identify any deficiencies in internal control over financial reporting that I consider to be material weaknesses as define above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Municipality of Patillas, Puerto Rico's financial statements are free of material misstatement, I performed test of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as item 2007-2.

I noted certain matters that I reported to management of Municipality of Patillas Puerto Rico in a separate letter dated October 31, 2007.

Municipality of Patillas, Puerto Rico's response to the findings identified in my audit is described in the accompanying schedule of findings and questioned costs. I did not audit the Municipality of Patillas, Puerto Rico's response and, accordingly, I express no opinion on it.

The report is intended solely for the information and use of management, Municipal Council 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.

Arecibo, Puerto Rico
October 31, 2007

The stamp number 2227523
was affixed to the
original of this report

JUAN A. FELICIANO CHARNECO
CONTADOR PUBLICO AUTORIZADO
LIC. No. 1263
PUERTO RICO
2227523
SELLO $5.00 $5.00

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

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND 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, 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, 2007. 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 of Municipality of Patillas compliance based on my audit.

I conducted my audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, "Audits of States and Local Governments". Those standards and OMB Circular A-133 require that I plan and perform the audit to obtain reasonable assurance about whether non-compliance 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 Municipality of Patillas' compliance with those requirements.

In my opinion, Municipality of Patillas, Puerto Rico, 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, 2007. However, the results of my auditing procedures disclosed instances of non compliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 2007-2.

Internal Control Over Compliance

The management of 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 the 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, but not for the purpose of expressing an opinion on the effectiveness of Municipality of Patillas internal control over compliance.

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

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

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

Municipality of Patillas' response to the findings identified in my audit are described in the accompanying schedule of findings and questioned costs. I did not audit Municipality of Patillas' Puerto Rico's response and, accordingly, I express no opinion on it.

This report is intended solely for the information and use of management, Municipal Council, others within the entity, 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.

Arecibo, Puerto Rico
October 31, 2007

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

The stamp number 2227524
was affixed to the
original of this report.

JUAN A. FELICIANO CHARNECO
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MUNICIPALITY OF PATILLAS, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2007

Federal Grantor / Pass-through Grantor Program Title	Federal CFDA Number	Pass-through Grantors Number	Federal Expenditures
U.S. Department of Housing and Urban Development			
Direct Program:			
Department of Housing and Urban Development Public and Indian Housing			
Section 8 - Voucher	14-871	RQ46-EO-57-001/002	$ 336,328
Section 8 - Existing	14-871	N/A	8,739
			345,067
Community Planning and Development	14-228	AB-2006	15,720
Community Development Block Grant (State Program)	14-228	AC-2005	93,750
Passed-through Commonwealth of Puerto Rico	14-228	FC-2005	299,098
Commissioners Office of Municipal Affairs	14-228	DR-2005	34,748
	14-228	AB-2004	20,626
	14-228	FC-2004	189,974
	14-228	AB-2003	105,077
	14-228	FC-2003	19,090
	14-228	AB-2002	3,020
	14-228	FC-2002	6,491
	14-228	2000	16,906
	14-228	1999	5,535
			810,035
			1,155,102
U.S. Department of Health and Human Services:			
Direct Program:			
Head Start	93-600	02CH9911/05	788,541
Passed-through Governors Office for Human Development:			
Administration for Children and Families			
Child Care and Development Block Grant	93-575	G0703PRCCDF	47,693
			836,234
U.S. Federal Emergency Management Agency (FEMA):			
Public Assitance Grant			
Passed-through Emergency Management State and Local Assistance			
FEMA (Lluvias noviembre)	83-544	N/A	2,520
U.S. Department of Agriculture			
Passed-through Commonwealth of Puerto Rico, Department of Education			
Child and Adult Care Food Program	10-558	PI-HS-06-02(CCC-198)	60,694
TOTAL FEDERAL ASSISTANCE			**$ 2,054,550**

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, 2007

(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 95% 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	$1,155,102	$836,234	$63,214	$2,054,550
State & Municipal Expenditures	-	-	1,304,430	1,304,430
Total Expenditures	$1,155,102	$836,234	$1,367,644	$3,358,980

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2007

A. Summary of Audit results

Financial Statements

Type of auditor's report issued:	Unqualified
Internal control over financial reporting:	
Material weakness (es) identified?	_____Yes __X__No
Reportable condition(s) identified not considered to be material weaknesses?	_____Yes __X__No None reported
Noncompliance material to financial statements noted?	_____Yes __X__No

Federal Awards

Internal control over major programs:	
Material weakness(es) identified?	____Yes _X__ No
Reportable condition(s) identified not Considered being material weaknesses?	___X__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	__X__Yes _____No

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2007

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
93.575	Child Care (Red de Cuido)

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

Auditee qualified as low-risk audit _____ Yes __X_ No

B - Financial Statements Findings

ACCOUNTING AND FINANCE DEPARTMENT

Ref. No. Finding / Noncompliance
---------- ----------
2007-01 Statement of Condition and Criteria

It was noted during my tests of internal control that monies were paid to a person not working in the Municipality.

We also noted that an employee transferred cash funds to her personal bank account.

A-102 Common Rule and OMB Circular A-110, require that non-Federal entities receiving Federal awards establish and maintain internal controls designed to reasonably ensure compliance with Federal laws, regulations and program requirements.

Law 81 of August 30, 1991, known as "Ley de Municipios Autónomos" establish that municipal employees perform with efficiency and diligence the tasks and functions assigned to their position. Chapter IV Section 9 (4) "Reglamento Revisado de Normas Básicas de OCAM" of July 31st, 1995.

Cause
The Municipality has deficiencies in its internal control procedures related to the processing of payroll. There are inadequate procedures related to the compilation and processing of payroll, assignment of employees between funds and programs, provisions for the safeguarding of assets, segregation of duties, and appropriate review by management.

Effect
The continued occurrence of this situation could result in misappropriation of funds affecting the municipality, and, if funds received from federal awards are involved, the Municipality could expend funds for unallowable activities which could result in disallowed costs by the Federal awarding Federal awarding agencies and the reduction or elimination of Federal grant awards.

Auditor's Recommendation
As a result of the above it is our recommendation that payroll processing procedures be reviewed and improved, including procedures for transfer of employees to department or programs, adequate segregation of duties between employees, improved review of the payroll before issuance by someone other than the payroll clerk, improved review of approved signatures on attendance cards, improved assignment of personnel to work on payroll processing.

We believe that segregation of duties and, thus internal control, could be improved if another management employee, such as the personnel manager, performs some of the procedures in the payroll process in order to improve internal controls in this area.

Municipality Response:
We concur with auditor's recommendations. The Municipality evaluates the actual administrative procedures to establish adequate procedures for the processing of payroll.

C – Federal Award Findings and Questioned Cost

Department of Housing and Urban Development
Public and Indian Housing (HUD)
CFDA No. 14-871
Grant No. Section 8 Voucher
Year ended June 30, 2007

Ref. No.	Finding / Noncompliance
2007-02	Statement of Condition and Criteria

It was noted in my test of compliance that the Municipality's financial management system did comply 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 HUD 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 as per Title 24 of CFR, part 84, Cc) (7).

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 and establish internal procedures to minimize the time elapsed to disburse the funds receive. The municipality should apply for an authorization from HUD to invest the excess of cash.

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 and will apply for an authorization from HUD to invest the excess of cash.

U.S. Federal Emergency Management Agency
Passed-through Emergency Management
State and Local Assistance
CFDA No. 83-544
Grant No. 1247 & 1552
Year ended June 30, 2007

Ref. No.	Finding / Noncompliance	Questioned Costs
2007-03	Statement of Condition and Criteria	

Effective control and accountability must be maintained for the grant. Administrative personnel must adequately safeguard all assets and must assure that it is used solely for authorized purpose, necessary and reasonable and allocate to federal award.

Cause
Internal control procedures of checks issued and controls were overridden by administrative personnel resulting in a misappropriation of funds.

Effect
Financial reports could include disbursements not allowable for the grant requirements.

Auditor's Recommendation
We recommend revising, improving and modifying the internal control procedures relative to disbursements to comply with program regulations and review the programs financial reports.

Municipality Response:
The administrative personnel determined questioned costs, reviewed and improve the payments procedure, reviewed the financial reports and claim the misappropriation of funds to the person responsible to recover the money. Misappropriated funds were reimbursed to the municipality by previous employee.

U.S. Department of Health and Human Services
Passed-through Governors Office for
Human Development
CFDA No. 93-575
Grant No. None Identified
Year ended June 30, 2007

Ref. No.	Finding / Noncompliance	Questioned Cost
2007-04	Statement of Condition and Criteria	

Effective control and accountability must be maintained for the grant. Administrative personnel must adequately safeguard all assets and must assure that it is used solely for authorized purpose, necessary and reasonable and allocate to federal awards.

Cause
Internal control procedures of checks issued and controls were overridden by administrative personnel resulting in a misappropriation of funds.

Effect
Financial reports could include disbursements not allowable for the grant requirements.

Auditor's Recommendation
We recommend revising, improving and modifying the internal control procedures relative to disbursements to comply with program regulations and review the programs financial reports.

Municipality Response:
The administrative personnel determined questioned costs, reviewed and improve the payments procedure, reviewed the financial reports and claim the misappropriation of funds to the person responsible to recover the money. Misappropriated funds were reimbursed to the municipality by previous employee.

MUNICIPALITY OF PATILLAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2007

2006 – Finding No. 1: 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, 2006
Finding was corrected

2006 – Finding No. 2: 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
Finding was corrected

2006 – Finding No. 3: U.S. Department of Housing and Urban Development
Public and Indian Housing
Section 8 – Voucher
CFDA NO. 14-871
Year ended June 30, 2006
Finding was corrected

2006 – Finding No. 4: U.S. Department of Housing and Urban Development
Public and Indian Housing
Section 8 – Voucher
CFDA NO. 14-871
Year ended June 30, 2006
Finding reported again.

CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2007
(continued)

Ref. No.	Finding /Corrective Action	Anticipated Completion Date
2007-01	Accounting and Finance Department	

Statement of Condition:
Effective controls and accountability

On or before end of 2007-08 fiscal year

It was noted in our test of internal control that controls and accountability are not complying with the requirements end laws applicable.

Corrective Action Planned:
The administrative controls for the issuance of checks, have been improved analysis and monitoring of the system were implemented to prevent irregularities. Financial reports were corrected and a claim to the person responsible for the misappropriation of funds. The Municipality are in the process of recovering the money from the person responsible.

Person Responsible:
Mr. Narciso Velázquez Rodríguez, Finance Director

Ref. No.	Finding /Corrective Action	Anticipated Completion Date
2007-02	Section 8 - Voucher:	

Statement of Condition:
The Section 8 voucher program cash balance over $5,000 for periods larger than 3 days.

On or before end of 2007-08 Fiscal year

Corrective Action Planned:
The Section 8 Voucher program Administration will evaluate and implement adequate procedures to control, use and invest in effective manner, federal funds.

Person Responsible:
Mr. Narciso Velázquez Rodríguez, Finance Director

GOBIERNO MUNICIPAL DE PATILLAS
OFICINA DE FINANZAS
APARTADO 698
PATILLAS, PUERTO RICO

CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2007
(continued)

Ref. No.	Finding /Corrective Action	Anticipated Completion Date
2007-03	FEMA Programs:	

Statement of Condition:
Effective Controls and accountability.

On or before end of 2007-08 Fiscal year

It was noted in our compliance test that the controls and accountability are not complying with the requirements and laws applicable.

Corrective Action Planned:
The administrative controls for the issuance of checks, have been improved. Analysis and monitoring of the system were implemented to prevent irregularities. Financial reports were corrected and a claim to the person responsible for the misappropriation of funds. The person responsible paid the whole amount of the funds taken.

Person Responsible:
Mr. Narciso Velázquez Rodríguez, Finance Director

Ref. No.	Finding /Corrective Action	Anticipated Completion Date
2007-04	Child Care:	

Statement of Condition:
Effective Controls and accountability.

On or before end of 2007-08 Fiscal year

It was noted in our compliance test that the controls and accountability are not complying with the requirements and laws applicable.

Corrective Action Planned:
The administrative controls for the issuance of checks, has been improved. Analysis and monitoring of the system were implemented to prevent irregularities. Financial reports were corrected and a claim to the person responsible for the misappropriation of funds. The person responsible paid the whole amount of the funds taken.

Person Responsible:
Mr. Narciso Velázquez Rodríguez, Finance Director

Narciso Velázquez Rodríguez