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**MUNICIPALITY OF PATILLAS, PUERTO RICO
SINGLE AUDIT REPORT
JUNE 30, 2010
(INDEPENDENT AUDITOR'S REPORT)**

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MUNICIPALITY OF PATILLAS, PUERTO RICO
SINGLE AUDIT REPORT
JUNE 30, 2010

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

Sr. Luis Acevedo
Finance Director

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Management's Discussion and analysis of the Municipality of Patillas (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2010. The Management Discussion and Analysis (MD & A) should be read in conjunction with the transmittal letter on page 9 and the Municipality's financial statements, which begin on page 12. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended June 30, 2010. This MD & A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with major information.

FINANCIAL HIGHLIGHTS

- The Net assets of the Municipality exceeded its liabilities at the close of the current fiscal year by \$11,551,210 net assets increased by \$1,653,433 when compared with prior year.
- Revenues were \$449,430 less than last year, while expenses were \$136,536 less than last year as reported in the Statement of Activities.
- The Municipality had reported in the General Fund a deficiency of revenues over expenditures amounting to \$1,618,145 in the accompanying statement of revenues.
- Loans principal payments were \$713,000 during fiscal year 2009-10. New bond issued were \$2,250,000, for payments of debts and public improvement.
- The actual revenues were \$8,755,647 and the expenditures were \$10,030,505 creating an excess of \$1,119,303 under the revenues in the Budgetary Schedule mainly due to unfavorable variances in revenues, (Municipal taxes).
- The Municipality government fund reported combined ending fund balances of \$3,572,591 in the accompanying statement of revenues, expenditures.
- The Municipality has reported a net undesignated fund balance deficit for the general fund amounting to \$1,717,932.

MUNICIPALITY OF PATILLAS MANAGEMENT'S DISCUSSION AND ANALYSIS

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.

The Property Tax revenue represents 13% of total revenues of the municipality during the last five years. The Municipal Revenue Collection Center (CRIM) of the Commonwealth of Puerto Rico 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.

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.

Governmental-wide financial statements - The government-wide financial statements which begin on page 12 of this report are designed to provide reads with a broad overview of the Municipality's finances, in a manner similar to a private-sector business. The government wide statements provide short and long term information about the municipality's status as a whole.

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.

MUNICIPALITY OF PATILLAS MANAGEMENT'S DISCUSSION AND ANALYSIS

The Statement of Net Assets and the statement of activities, on page 12-13, 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 valued and reported within the Governmental column of the Governmental Wide Statement. Additionally, the government must elect to either depreciate these assets over their estimated useful life or develop a system of assets management designated to maintain the service delivered potentially to near perpetuity. If the government develops the assets management system, which periodically, by category, measures and demonstrate its maintenance system, which periodically, by category, measures and demonstrate its maintenance of locally established level of services standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statements users in evaluating a local government and its performance over time.

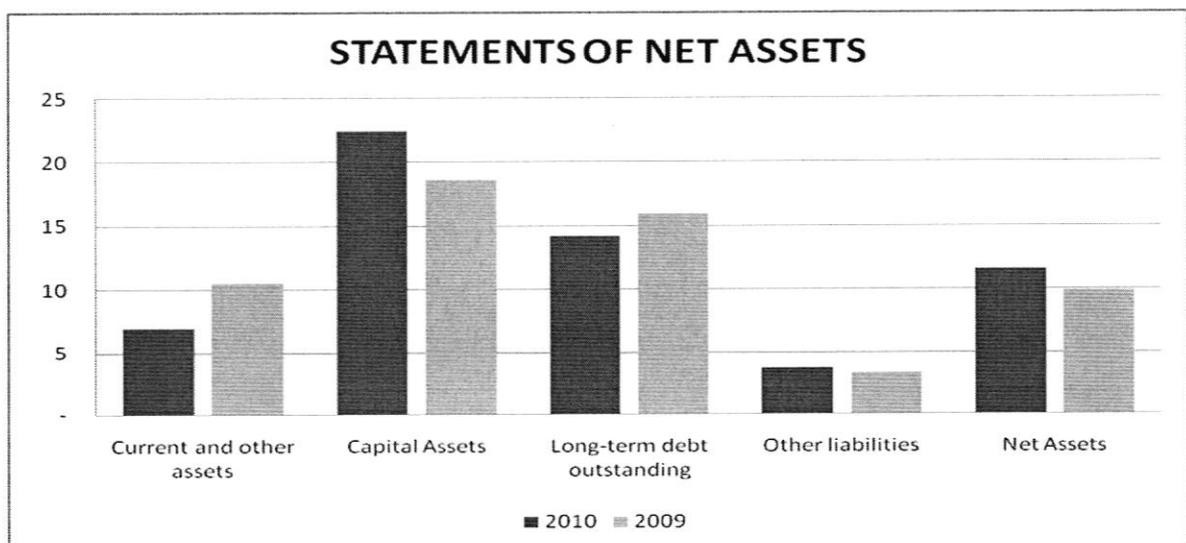
**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

**Government-Wide Financial Analysis
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 \$11,551,210 at the close of the recent fiscal year compare to \$9,897,757 at the end of previous year, as restated and showed in the following condensed Statement of Net Assets of the Primary Government.

**Statements of Net Assets
As of June 30, 2010 and 2009**

	2010	2009	Changes	%
Current and other assets	\$ 6,954,054	\$ 10,492,584	\$ (3,538,530)	-34%
Capital assets net	22,455,697	18,654,851	3,800,846	20%
Total assets	29,409,751	29,147,435	\$ 262,316	0.01
Current and other liabilities	3,677,521	3,261,427	416,094	13%
Long-term liabilities	14,181,020	15,988,251	(1,807,231)	-11%
Total liabilities	17,858,541	19,249,678	(1,391,137)	-7%
Net assets:				
Invested in capital assets, net of related debt	16,553,546	11,896,454	4,657,092	39%
Debt service		(162,114)	162,114	-100%
Special and other funds	1,278,227	312,740	965,487	309%
Capital project fund	4,012,296	7,683,799	(3,671,503)	-48%
Unrestricted (deficit)	(10,292,859)	(9,833,122)	(459,737)	5%
Total net assets	\$ 11,551,210	\$ 9,897,757	\$ 1,653,453	17%



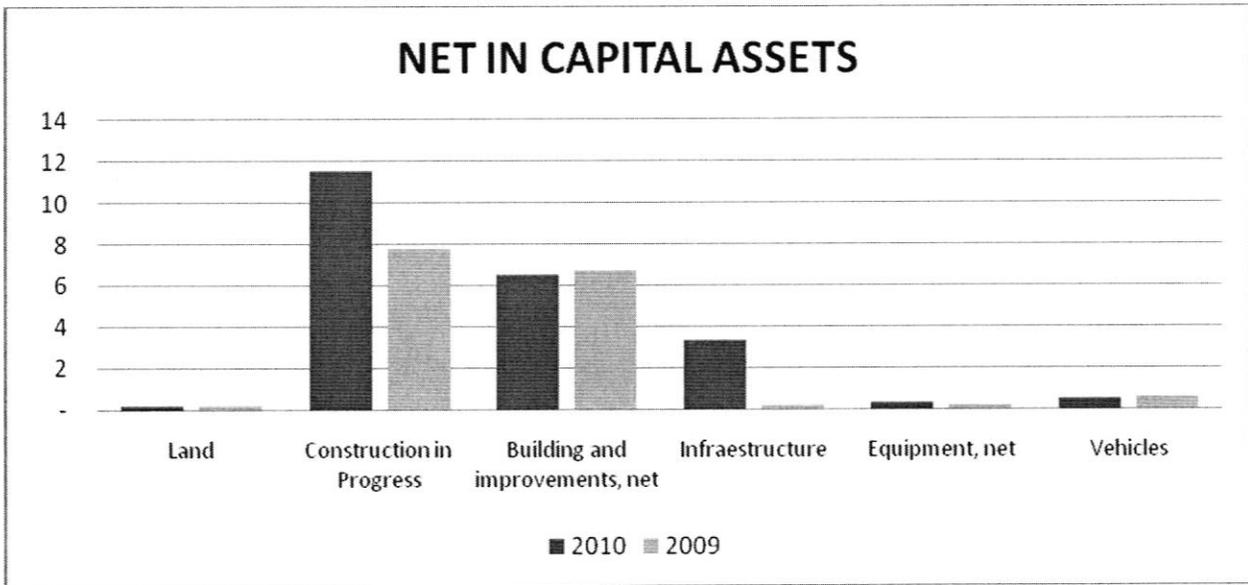
**MUNICIPALITY OF PATILLAS
MANAGEMENT'S DISCUSSION AND ANALYSIS**

The decrease of \$3,538,530 in current net asset was mainly due to decrease of cash and investment of \$7,008,157. The account Capital assets increased by \$3,800,846 principally by additions to construction in progress of \$3,777,390, at the same time created increased in the net investment in capital asset of \$4.6 million and the Capital Project Fund decrease by \$3.6 million.

Current liabilities increase by 13 percent caused by a increase of accounts payable of \$1.5 million. Long-term liabilities decrease by \$1.8 million is reflected principally in the Obligation Bonds payments of \$2.2 million.

Increase (Decrease) Net in Capital Assets was as follows:

	6/30/2010	%	6/30/2009	%	Change
Land	\$ 192,199	1%	\$ 192,199	1%	\$ -
Construction in progress	11,555,176	52%	7,777,786	42%	3,777,390
Building and improvements, net	6,537,733	29%	6,716,958	36%	(179,225)
Infrastructure	3,326,276	15%	3,244,538	17%	81,738
Equipment, net	305,264	1%	172,003	1%	133,261
Vehicles	539,049	2%	551,367	3%	(12,318)
Total Net Capital Asset	\$ 22,455,697		\$ 18,654,851		\$ 3,800,846



Building improvements net represent 22 percent and 29 percent of total asset and net capital assets respectively. Construction in progress represents 39 percent of total asset and 52 percent and net capital asset. The Increase in Construction in progress by \$3.8 million when compared with prior year, includes \$81,738 increase in infrastructure.

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

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

**Statements of Activities
For the year ended June 30, 2010 and 2009
Changes in Net Assets**

	2010	2009	Changes	%
General Revenues	\$ 10,366,253	\$ 10,187,855	\$ 178,398	2%
Program Revenues	3,451,633	4,079,461	(627,828)	-15%
Total Revenues	13,817,886	14,267,316	\$ (449,430)	-3%
Expenses				
Governmental activities	(12,164,433)	(12,477,327)	312,894	-3%
Changes in net assets	\$ 1,653,453	\$ 1,789,989	\$ (136,536)	-8%

The Statement of Activities reflects for fiscal year 2010, the net effect of revenues derived from several programs plus current operating revenues. Total revenues compared to the total expenses, amounted to a decrease of \$136,536 in the Municipality's net assets. Approximately 26 percent of the Municipality's total revenue came from taxes, while 24 percent resulted from Federal grants and 47 percent resulted from Intergovernmental Revenues. The Municipality's expenses cover a range of services like health, public safety, sanitation, recreation and sports, education, housing, transportation, welfare, construction and improvements. The largest expenses were for general government, public works, education and training and culture and recreation. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

A brief review of the Statements of Activities of the Municipality at June 30, 2010, shows total expenses incurred to afford the cost of all functions and programs amounted to \$8,712,800. Upon examining the sources of revenues for the financing of the programs, the Statement reflects the following; \$1,100,797 from operating grants and contributions; and \$2,350,836 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$10,366,253. There was a change in net assets \$1.6 million that represents 15 per cent of total revenues and a decrease of 8 percent when compared with prior year. Expenses decrease by \$312,894 or 5 percent when compared with prior year.

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

FINANCIAL ANALYSIS OF THE GOVERNMENTAL FUNDS

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

**Governmental Funds
Balance Sheets
June 30, 2010 and 2009**

	2010	2009	Changes	%
Assets:				
Cash	\$ 2,336,263	\$ 9,344,420	\$ (7,008,157)	-75%
Restricted Cash	4,356,493	479,585	3,876,908	808%
Accounts Receivable	3,916,636	3,460,646	455,990	13%
Total Assets	\$ 10,609,392	\$ 13,284,651	\$ (2,675,259)	-20%
Liabilities and Fund Balance				
Liabilities:				
Total Liabilities	\$ 7,036,801	\$ 4,621,617	\$ 2,415,184	52%
Funds Balances	3,572,591	8,663,034	(5,090,443)	-59%
Total liabilities and Fund Balances	\$ 10,609,392	\$ 13,284,651	\$ (5,090,443)	-38%

The Fund Financial Statement is another important component of the Municipality's financial statements. A fund is a grouping of related accounts is used to maintain accountability and controls over economic resources of the Municipality that have been segregated for specific activities. The Municipal fund type of accounting is used to demonstrate compliance with related legal requirements. Information offered thru this Statement is limited to the Municipality most significant funds and is particularly related to the local government only instead of the government as a whole. Government funds are used to account for essentially the same functions as those reported as governmental activities.

During the year 2010 the municipality had \$4.3 million cash restricted in the Bond issued Fund and Debt service fund and in 2010 the Due to special revenue were increased by \$2.4 million. Deferred revenues decreased by \$94,554.

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

**Statements of Revenues, Expenditures and Changes in Fund Balances
Years Ended June 30, 2010 and 2009**

	2010	2009	Changes	%
Revenues:				
Property taxes	\$ 1,776,030	\$ 1,567,062	\$ 208,968	13%
Volume of business tax	545,617	567,076	(21,459)	-4%
Intergovernmental revenue	6,526,435	5,713,230	813,205	14%
Federal grants	3,451,633	4,574,801	(1,123,168)	-25%
Sales Tax	963,864	819,050	144,814	18%
Other	554,307	1,521,097	(966,790)	-64%
Total Revenues	\$ 13,817,886	\$ 14,762,316	\$ (944,430)	-6%
Liabilities and Fund Balance				
Expenditures:				
General Government	\$ 4,774,973	\$ 6,183,415	\$ (1,408,442)	-23%
Public safety and public work	3,984,833	3,436,225	548,608	16%
Education and training and culture	2,266,109	1,875,014	391,095	21%
Capital outlays	4,142,092	1,859,480	2,282,612	123%
Other	383,942	366,419	17,523	5%
Bonds (principal and interest)	1,126,695	773,920	352,775	46%
Total Expenditures	\$ 16,678,644	\$ 14,494,473	\$ 2,184,171	15%
Prior period Adjustment		789,421		
Excess of revenues (expenditures)				
Over expenditures (revenues)	\$ (2,860,758)	\$ 267,843	\$ (3,128,601)	-1168%
Fund Balance, ending	\$ 3,572,591	\$ 8,663,034	\$ (5,090,443)	-59%

The most significant changes of this statement were as follows:

- (1) Revenues from property tax were increased by \$208,968 due to increase in property tax in the amount collected. The increase in Intergovernmental revenue of \$813,205. Revenue from volume business tax declaration were reduce by \$21,459 on funds received when compared with prior year, reflected in sales reported in the municipal tax declaration was reduce approximately by 3 per cent in many taxpayer. Other revenues decrease by \$1 million, principally for eventual income.

Expenditures were increase by approximately \$2.2 million in Capital outlays expense when compared with the prior year. The total expenditures increased by \$1.8 million, principally in Capital outlays, and all other expenses by \$1.3 million, except general government decreased by \$1.7 million. The payments of all debts are preliminary approved on October 14, 2010 by the Government Development Bank by the issuance of Bonds General Obligations from Municipal Redemption Fund and the Municipal Development Fund. The Municipality won the civil case GCD-1999-0210 to Centro de Servicios Primarios de Salud for the amount of \$2,131,052. The Municipality is waiting for the execution of the sentence to cover the Municipal operational debts.

Estado Libre Asociado de Puerto Rico

Gobierno Municipal del Pueblo de Patillas

Sr. Luis Acevedo
Finance Director

MUNICIPALITY OF PATILLAS MANAGEMENT'S DISCUSSION AND ANALYSIS

Economic Factors and Next Year Budget

The Municipality is a political legal entity with full legislative and administrative powers in every area of municipal government, with perpetual existence and legal personality, separate and independent from the central government 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 Budget for Revenues and expenditures were \$9.3 million for the general fund, total revenues decreased \$548,205 when compared the budgeted revenues with the actual revenues. Municipal license tax decreased by \$124,883 and excise tax by \$204,557. The actual expenditure were \$571,098 more than budgeted expenditures. General Government reflected an increase of \$207,093, and Public Works \$207,624 when compared Budget Expenditures with actual expenditures. Excess of revenues under expenditures reflect a decrease of \$1,119,303, mentioned in this paragraph

The Municipality has finished during the year the Reconstruction of the La Felicita Bridge and improvements in Bo. Mulas, Bo. Apeadero, Bo. Mamey and Bo. Marín. The Municipality construction in process include the Construction of recreational facility in Lake Patillas, Public Car Terminal, the New Market Square, the Nestor Vazquez Court, Roof of Villas de Patillas Court, and other 65 projects in process.

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.

Luis Acevedo, Finance Director, PO Box 698, Patillas, PR 00723. Telephone (787)839-4120 Fax: (787) 839-9546 E-mail: finanzas1@prtc.net

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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, 2010, 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 did not audit the financial statement of the Esmeralda del Sur which is shown as discretely presented component unit. That statement was audited by other auditors whose reports has been furnished to us, and my opinion, insofar as it release to the amount included for Esmeralda del Sur, is based solely on the report of the other auditors.

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, based on my audit and reports of the other auditors, 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, 2010, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, I have also issued my report dated December 17, 2010 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 my 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 schedules information on pages 1 through ⁹7 and page ¹⁷15, 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
December 17, 2010

The stamp number 2541928
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original of this report.


CPA JUAN A. FELICIANO CHARNECO
License No. 1263
Expires December 1, 2013

MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF NET ASSETS
JUNE 30, 2010

<u>ASSETS</u>	<u>Primary Government Governmental Activities</u>	<u>Component Unit Esmeralda Del Sur</u>
Cash and investments	\$ 2,336,263	\$ 104,451
Cash with fiscal agent and restricted deposit	4,356,493	1,186,608
Accounts receivable other	-	8,457
Accounts receivable from federal government	82,304	-
Accounts receivable from government	178,994	-
Capital assets, net of accumulated depreciation	22,455,697	1,508,565
Other assets	-	29,513.00
Total assets	\$ 29,409,751	\$ 2,837,594
 <u>LIABILITIES</u>		
Liabilities:		
Accounts payable and accrued liabilities	\$ 1,314,543	\$ 41,770
Due to government entity	962,149	-
Deferred revenue (volume business tax)	304,704	-
Noncurrent liabilities:		
Due within one year	1,096,125	119,261
Due in more than one year	14,181,020	48,500
Mortgages payable	-	1,008,742
Total liabilities	17,858,541	1,218,273
 <u>NET ASSETS</u>		
Invested in capital assets, net of related debt	16,553,546	380,562
Restricted for:		
Reserve for debt service	-	-
Special and other fund	1,278,227	1,186,608
Capital project fund	4,012,296	-
Unrestricted (Deficit)	(10,292,859)	52,151
Total net assets	11,551,210	1,619,321
Total Liabilities and net Assets	\$ 29,409,751	\$ 2,837,594

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

Functions/Programs	Program Revenues		Net (Expenses) Revenues and Changes in net assets	
	Charges for Services	Capital Grants and Contributions	Operating Grants and Contributions	Component Unit
	Expenses			Esmeralda del Sur
EXPENDITURES:				
General government	\$ 4,813,840	\$ (2,350,836)	\$ (191,937)	\$ -
Public safety	3,064,143	-	-	3,064,143
Public works	1,218,805	-	-	1,218,805
Health	384,436	-	-	384,436
Culture and recreation	1,354,859	-	-	1,354,859
Education and training	915,020	-	(908,860)	6,160
Interest on long -term debt	413,330	-	-	413,330
Total governmental activities	\$ 12,164,433	\$ (2,350,836)	\$ (1,100,797)	\$ 8,712,800
Component units:				
Esmeralda del Sur	496,733	-	-	496,733
Total component unit	\$ 496,733	-	-	\$ 496,733
GENERAL REVENUES:				
Property taxes			1,776,030	-
Municipal licenses tax			545,617	-
Licenses, permits and fines			398,443	-
Intergovernmental revenues			6,526,435	-
Rent of properties			67,064	547,891
Interest revenues			49,970	-
Other revenues			38,830	1,507
Municipal sales tax			963,864	-
Financial			-	42,987
Total general revenues			10,366,253	592,385
Changes in net assets			1,653,453	95,652
Net assets at beginning of year			13,059,386	1,523,669
Prior period adjustment (Note 18)			(3,161,629)	-
Net assets at end of year			\$ 11,551,210	\$ 1,619,321

See notes to financial statements.

**MUNICIPALITY OF PATILLAS, PUERTO RICO
BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2010**

	General Fund	Bonds Issue Fund	HUD Programs	Head Start Programs	Homeland Security Programs	Debt Service Fund	Other Funds	Total Governmental Funds
ASSETS								
Cash and investments	\$ 427,519	\$ -	\$ 148,566	\$ 8,234	\$ 395,751	\$ -	\$ 1,356,193	\$ 2,336,263
Cash with fiscal agent	-	3,581,912	-	-	-	774,581	-	4,356,493
Account receivable (volume business tax) and other	56,818	-	-	-	-	25,486	-	82,304
Accounts receivable from federal government	-	-	80,295	23,537	75,162	-	-	178,994
Due from other funds	1,701,858	-	-	-	-	-	1,953,480	3,655,338
Total assets and other debits	\$ 2,186,195	\$ 3,581,912	\$ 228,861	\$ 31,771	\$ 470,913	\$ 800,067	\$ 3,309,673	\$ 10,609,392

LIABILITIES AND FUND BALANCES

Liabilities:								
Accounts payable and accrued liabilities	\$ 683,794	\$ -	\$ 56,086	\$ 24,099	\$ 102,204	\$ 800,067	\$ 448,360	\$ 2,114,610
Due to special revenue and general fund	1,953,480	-	63,119	6,576	-	-	1,632,163	3,655,338
Due to government entities	962,149	-	-	-	-	-	-	962,149
Deferred revenue (volume business tax)	304,704	-	-	-	-	-	-	304,704
Total liabilities	3,904,127	-	119,205	30,675	102,204	800,067	2,080,523	7,036,801
Fund balances:								
Reserve for debt services	-	-	-	-	-	-	-	-
Encumbrances	390,118	-	-	-	-	-	-	390,118
Undesignated	(2,108,050)	-	-	-	-	-	-	(2,108,050)
Special and other funds	-	-	47,981	1,096	-	-	1,229,150	1,278,227
Capital project fund	-	3,581,912	61,675	-	368,709	-	-	4,012,296
Total fund balances	(1,717,932)	3,581,912	109,656	1,096	368,709	-	1,229,150	3,572,591
Total liabilities and fund balance	\$ 2,186,195	\$ 3,581,912	\$ 228,861	\$ 31,771	\$ 470,913	\$ 800,067	\$ 3,309,673	\$ 10,609,392

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

TOTAL FUND BALANCE - GOVERNMENTAL FUNDS	\$ 3,572,591
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	22,455,697
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	\$ 936,286
Bonds payable	10,438,000
Legal claims	73,928
Accrued governmental expense	3,028,864
Total Long-Term Debt Liabilities	\$ 14,477,078
TOTAL NET ASSETS OF GOVERNMENTAL ACTIVITIES	\$ 11,551,210

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, 2010

	General Fund	Bonds issue Fund	HUD Programs	Head Start Programs	Homeland Security Programs	Debt Service Fund	Other Funds	Total Governmental Funds
REVENUES:								
Property taxes	\$ 1,314,571	-	-	-	-	\$ 461,459	-	\$ 1,776,030
Municipal license tax	545,617	-	-	-	-	-	-	545,617
Licenses, permits, fines and sales tax	398,443	-	-	-	-	-	-	398,443
Intergovernmental revenues	5,334,301	-	-	-	-	-	1,192,134	6,526,435
Rent of properties	67,064	-	-	-	-	-	-	67,064
Interest income	44,601	-	-	-	-	5,369	-	49,970
Other revenues	38,830	-	-	-	-	-	-	38,830
Municipal sales tax	619,037	-	-	-	-	344,827	-	963,864
Federal financial award	-	-	1,468,891	908,860	881,945	-	191,937	3,451,633
Total revenues	8,362,464	-	1,468,891	908,860	881,945	811,655	1,384,071	13,817,886

EXPENDITURES:								
Current:								
General government	4,240,517	-	534,151	-	305	-	-	4,774,973
Public safety	3,060,841	-	-	-	-	-	-	3,060,841
Public works	923,992	-	-	-	-	-	-	923,992
Health	383,942	-	-	-	-	-	-	383,942
Capital outlays	20,228	1,916,126	905,371	-	998,641	-	301,726	4,142,092
Culture and recreation	1,351,089	-	-	-	-	-	-	1,351,089
Education and training	-	-	-	915,020	-	-	-	915,020
Debt service:								
Principal retirement	-	-	-	-	-	713,000	-	713,000
Interest and fiscal charges	-	-	-	-	-	413,695	-	413,695
Total expenditures	9,980,609	1,916,126	1,439,522	915,020	998,946	1,126,695	301,726	16,678,644
Excess of revenues over (under) expenditures	(1,618,145)	(1,916,126)	29,369	(6,160)	(117,001)	(315,040)	1,082,345	(2,860,758)

OTHER FINANCING SOURCES (USES):								
Transfer in (out) to debt service fund	(526,555)	-	-	-	-	526,555	-	-
Transfer in (out)	450,000	-	-	-	-	(450,000)	-	-
Interest Expenditure	-	-	-	-	-	365	-	365
Bond Expenditure	-	(2,230,050)	-	-	-	-	-	(2,230,050)
Total other financing sources (uses)	(76,555)	(2,230,050)	-	-	-	76,920	-	(2,229,685)
Excess of revenues over (under) expenditures and other uses and other sources	(1,694,700)	(4,146,176)	29,369	(6,160)	(117,001)	(238,120)	1,082,345	(5,090,443)
Net change in fund balances	(1,694,700)	(4,146,176)	29,369	(6,160)	(117,001)	(238,120)	1,082,345	(5,090,443)
Fund balance June 30, 2009	39,188	7,594,883	45,802	7,256	-	162,114	348,598	7,873,613
Prior period adjustment (Note 18)	(62,429)	133,205	34,485	-	485,710	400,234	(201,793)	789,421
Fund balance June 30, 2010	\$ (1,717,942)	\$ 3,581,912	\$ 109,656	\$ 1,096	\$ 368,709	\$ -	\$ 1,229,150	\$ 3,572,591

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See notes to financial statements.

**MUNICIPALITY OF PATILLAS
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
JUNE 30, 2010**

Net change in fund balance - total governmental funds \$ (5,090,443)

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

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	4,142,092	
Less: current year depreciation	<u>(341,246)</u>	
		3,800,846

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

Principal payments	713,000	
Bond expenditure	<u>2,230,050</u>	
		2,943,050

Change in net assets of governmental activities \$ 1,653,453

See notes to financial statements.

MUNICIPALITY OF PATILLAS, PUERTO RICO
BUDGETORY COMPARISON SCHEDULE GENERAL FUND (BUDGET BASIS)
GENERAL FUND AND DEBT SERVICE
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

	Budgeted Amounts		Adjusted Actual Note 1	Variance Favorable (Unfavorable)
	Original	Final		
REVENUES:				
Property taxes	\$ 298,686	\$ 298,686	\$ 298,686	\$ -
Municipal license tax	670,500	670,500	545,617	(124,883)
Intergovernmental revenues	5,058,546	5,058,546	5,334,301	275,755
Licenses, permits and fines	603,000	603,000	398,443	(204,557)
Municipal sales tax	840,000	840,000	619,037	(220,963)
Rent of properties	100,000	100,000	67,065	(32,935)
Interest income	163,200	163,200	44,601	(118,599)
Other revenues	610,853	610,853	488,830	(122,023)
Other sources	959,067	959,067	959,067	-
Total revenues	\$ 9,303,852	\$ 9,303,852	\$ 8,755,647	\$ (548,205)
EXPENDITURES:				
Current:				
General government	\$ 3,184,422	\$ 3,576,993	\$ 3,784,086	\$ (207,093)
Public safety	988,975	940,471	923,992	16,479
Public Works	3,122,218	2,853,217	3,060,841	(207,624)
Health	441,863	426,512	383,942	42,570
Culture and recreation	1,278,674	1,375,014	1,351,089	23,925
Transfer to debt service	287,200	287,200	526,555	(239,355)
Total expenditures	\$ 9,303,352	\$ 9,459,407	\$ 10,030,505	\$ (571,098)
Excess of revenues over (under) expenditures		\$ (155,555)	\$ (1,274,858)	\$ (1,119,303)
Explanation of differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 8,755,647
Differences - budget to GAAP:				
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes.				(450,000)
Revenue accrued for financial purpose only				56,817
Total revenues as reported on the statement of revenue, expenditure, and changes in fund balances				\$ 8,362,464
Uses/outflow of resources				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 10,030,505
Differences - budget to GAAP:				
Non budgeted expenditures				962,149
Budgeted expenditures included prior year				(485,490)
Transfer to debt service				(526,555)
Total expenditures as reported on the statement of revenue, expenditures and change in fund balances				\$ 9,980,609

See notes to budgetary comparison schedule.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

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 (14) 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 implemented this Standard for the fiscal year ended June 30, 2004.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

b. Reporting Entity

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential components units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, "The Financial Reporting Entity" of the GASB. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government appoints a voting majority of the entity's governing body, and if either one of the following conditions exists: the primary government can impose its will on the other entity or the potential exist for the other entity to (1) provide specific financial to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the components unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

The reporting entity is composed of the primary government and its component unit, which is included to ensure the financial statements are not misleading.

Discretely Presented Component Units

The following discretely presented component unit is in the basic financial statement because of the nature of the services they provide and the Municipality's ability to impose its will.

Municipality of Patillas Component Unit – Esmeralda Del Sur

Esmeralda del Sur (the Project) is a housing development project consisting of land, and twelve one-story concrete building and other improvements owned by the Municipality of Patillas. The Project leases its 100 rental units to and/or low and moderate income individuals in the Patilla's area. Project Esmeralda del Sur is located at "Calle los Colegios, Patillas, PR 00723".

The Project is governed by board of directors that are appointed by the Municipality's Legislative Assembly. The mayor of the Municipality is a permanent member of the board of directors.

The following is relevant information extracted from the financial statements of the Project.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

b. Reporting Entity

Summary of significant accounting policies:

The following summarizes the major accounting policies judged by management to be the most appropriate in the circumstances to present fairly the Project's financial position, results of operations and cash flows in conformity with generally accepted accounting principles.

Federally subsidized rent income – The Project is under financing from Rural Housing Service (RHS) under Section 515 of the Housing Act of 1949. The properties are operated subject to Section 8 Housing Assistance Payments agreement with the U.S. Department of Housing and Urban Development (HUD), and a portion of the Project's rental income is received from HUD. The agreement was effective on April 1, 1979, with an initial term of five years and extended at the project's opinion for additional five years term and seven additional five years renewal option through the year 2019 to make housing assistance payments. HUD has agreed to pay the Project the difference between the contract rent, as defined in the agreement, and that portion of rent payable by qualified tenants. In addition, HUD has agreed to pay a portion of the contract rent to the project during certain vacancy periods.

Cash and Restricted Deposits

Under the term of the HAP contract the Project is required to set aside specified amounts for the replacements of property and other project expenditures approved by HUD. HUD restricted deposits, which approximate \$1,186,608 at June 30, 2010, are held in separate account and generally are not available for operating purpose.

The Project maintains a restricted cash accounts fir insurance escrow. In additions, all tenant security deposits are deposited into a separate bank account and held in trust for the tenants until they vacate the property. Any amounts not returned to the tenant due to lease violations are transferred to the Project's general operating accounts. Restricted funds are held in separate accounts and are not available for operating purpose.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

b. Reporting Entity (continuation)

Mortgage Payable

Consists of a 9% (with an effective subsidy rate of 8%) mortgage note used for construction of the projects buildings, payable in monthly installments of \$16,757, including interest, until 2017, collateralized with land and building.

The principal maturities of the mortgage in each of the next five years are:

<u>Year ending June 30</u>	<u>Amount</u>
2011	\$ 119,261
2012	130,449
2013	142,686
2014 and	156,071
there after	579,537
	<u>\$ 1,128,004</u>

Pollution remediation obligation

Based on comprehensive Asbestos-Containing Material (ACM) survey engaged by the project's management agent, it was determined that the project's buildings contain asbestos materials. These materials need to be removed in accordance with Puerto Rico Environmental Quality Board (EQB) regulation with the use of proper engineering controls.

At June 30, 2010 the project has accrued its best estimates of its obligation regarding the removal of asbestos materials, which is presented under the pollution remediation obligation caption in the accompanying balance sheet. The estimated liability of \$48,500 was obtained from the project's comprehensive asbestos-containing materials (ACM) survey. It is reasonably possible that the recorded estimate of the obligation may change in the near term.

Management fees

During the year ended June 30, 2010 the management agent's compensation is based in an amount equal to twenty-nine dollars (\$29) per unit per month. The management agent is Housing Promoters, Inc.

Complete financial statements for the individual component unit may be obtained from their administrative office located at "Calle los Colegios, Patillas, PR 00723".

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

c. Basic Financial Statements-GASB Statement No. 34

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

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

This government-wide focus is more on the sustainability of **the Municipality** as an entity and 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 sources 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 based financial statements into the governmental column of the government-wide presentation.

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 of major funds. **The Municipality** reports the following major funds on **Fund Financial Statements**:

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)**

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

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.

Bond Issue Fund – Bond Issue fund are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified.

Homeland Security Programs – Special revenue fund for revenue from the grant are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified.

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.

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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

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.

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

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

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

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 balances 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 the following 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:

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 \$155,555.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

g. Budgetary Data (continuation)

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.

Legal Compliance

Article 7.003, Law No. 81 of August 31, 1991, amended require that Mayor provide to Municipal Legislature an annual balanced budge indicating: 1) interest, amortization and retirement public debt, 2) statutory obligations, 3) judicial claims payments, 4) any amount to cover prior years deficit, 5) contract commitments and operational expenditures. For annual interest and principal debt amortization, CRIM provides annual estimated resources that will be obtained of additional special property tax (municipal) collections. **The Municipality's** management shows budgetary financial statements in general and debt service funds in compliance with state law and which are based in annual activity. The legal level of budgetary control is at the individual department level for general fund (Mayor and Legislature funds) expenditures, and annual principal and interest due for debt service fund.

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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

i. Inventories

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

j. Capital Assets

Fund Financial Statements

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

Government Wide Financial Statement

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

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

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 leave 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**.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

m. Restricted Assets

Investments and Certificates

Certain proceeds of the Municipality revenue bonds 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. In debt service fund are unsecured and collateralized, as no collateral is required by governmental banks.

n. Reservations of Fund Balance

Undesignated- fund balance available any purpose.

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.
- *Reserve for Debt Service* – Represents net assets available to finance future debt service payments.
- *Capital Projects Fund* – Represent net assets available to finance future capital outlays.
- *Homeland Security* – Represent net assets available to finance future capital outlays.
- *Special Revenue Fund* – Represent net assets available to finance specified outlays.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continuation)

n. Reservations of Fund Balance (continuation)

- *Special and Other Funds* – 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 affect 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 not been made.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

2. PROPERTY TAXES

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

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

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

The tax rate per annum is 10.33% for real property and 8.33% for personal property of which 8.33% 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.

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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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

2. PROPERTY TAXES (Continuation)

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 \$45,343 during 2010.

The following is a summary of the property tax advances that resulted in an Accounts Receivable, to the year ended June 30, 2010. The resulting receivable is presented in the general fund for Fund Financial Statement and is presented as revenue in both Financial Statements.

Accounts Receivable:

Amortization through collections of property taxes by the CRIM	
07-01-09 - 06-30-10	\$ 5,453,667
Advance received, 07-01-09 - 06-30-10	(5,425,489)
Sub-Total	28,178
** Amount Debt to Municipality	28,640
Accounts Receivable - 2010	\$ 56,818

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

3. DEPOSITS

The Municipality's cash and investments at June 30, 2010, were entirely covered by the Federal Depository Insurance Corporation by collateral provided by the banks and held by the Department of the Treasury pursuant to applicable laws and regulations. Cash with fiscal agent is maintained in interest-bearing accounts in the Government Development Bank for Puerto Rico and is collateralized by the Commonwealth of Puerto Rico.

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

4. CONCENTRATION OF CREDIT RISK

The Municipality maintains its cash account in local commercial banks, whose accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. Deposits in excess of \$250,000 are collateralized by the bank securities to property safeguard such funds. Nevertheless, management believes that concentration of credit risk is limited because balances are deposited with high standing financial institutions.

5. MUNICIPAL LICENSE TAXES

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

The tax rates are as follow:

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

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

The deferred revenue of the general fund correspond to the business tax levied received from the next fiscal year.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

5. MUNICIPAL LICENSE TAXES (Continuation)

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, 2010 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 balances are as follows:

Funds	Due From	Due To
General	\$ 1,701,858	\$ 1,953,480
Head Start Programs	-	6,576
Other funds	1,953,480	1,632,163
HUD Programs	-	63,119
TOTAL	\$ 3,655,338	\$ 3,655,338

For the most part, the effect of interfund activity has been removed from the 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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

8. DUE TO GOVERNMENTAL ENTITIES

As of June 30, 2010 balances due to governmental entities of the general fund consists of the following:

Name	Current Due to	Wide Fiancial Statements
Puerto Rico Retirement System	\$ 283,963	\$ 624,027
Puerto Rico Water Authority	118,790	430,810
Puerto Rico Department of Labor	103,525	425,028
Internal Revenue Service Center	138,290	805,851
Puerto Rico Department of treasury	287,711	564,565
Puerto Rico Employee Association S.	-	89,626
State Insurance Fund Corp.	29,116	-
Puerto Rico Telephone company	754	-
General Administration Services	-	88,957
TOTAL	\$ 962,149	\$ 3,028,864

The Municipality refinances the accounts payable for governmental expenditures and other accounts payable to Long-Term basis. The Municipality has the intention with the Government Development Bank to finance the governments debts with a General Obligation Bond used to pay Internal Revenue Service Center, Puerto Rico Department of Labor, Puerto Rico Retirement System, Department of Treasury, General Administration Service and Puerto Rico Employee Association System.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

9. CAPITAL ASSETS

Include those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation.

Capital assets activity for the year ended June 30, 2010 was as follows:

	Balance 6/30/2009	Additions	Retire- ments	Balance 6/30/2010
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 192,199	\$ -	\$ -	192,199
Construction in progress	7,777,786	3,777,390	-	11,555,176
Total capital assets not being depreciated	<u>7,969,985</u>	<u>3,777,390</u>	<u>-</u>	<u>11,747,375</u>
Capital assets, being depreciated				
Buildings and building improvements	10,736,950	-	-	10,736,950
Infraestructure	3,297,917	116,978	-	3,414,895
Equipment	1,100,017	149,604	-	1,249,621
Vehicles	3,793,528	98,120	-	3,891,648
Total capital assets being depreciated	<u>18,928,412</u>	<u>364,702</u>	<u>-</u>	<u>19,293,114</u>
Less: accumulated depreciation for:				
Buildings and building improvements	4,019,992	-	179,225	4,199,217
Infraestructure	53,379	-	35,240	88,619
Equipment	928,014	-	16,343	944,357
Vehicles	3,242,161	-	110,438	3,352,599
Total accumulated depreciation	<u>8,243,546</u>	<u>-</u>	<u>341,246</u>	<u>8,584,792</u>
Total capital assets being depreciated, net	<u>10,684,866</u>	<u>364,702</u>	<u>(341,246)</u>	<u>10,708,322</u>
Governmental activities capital assets, net	<u>\$ 18,654,851</u>	<u>\$ 4,142,092</u>	<u>\$ (341,246)</u>	<u>\$ 22,455,697</u>

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

Governmental activities:	
General government	\$ 38,867
Public works	294,813
Public safety	3,302
Culture and recreation	3,770
Health	494
Total depreciation expense governmental activities	\$ 341,246

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

9. CAPITAL ASSETS (Continuation)

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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

10. CHANGES IN GENERAL LONG-TERM DEBT

General in General Long – Term Debt

The principal long-term obligation of the Municipality is obligation bonds issue to pay governmental debts and accounts payable. 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, 2010.

Description	Beginning Balance	Additions	Reductions	Ending Balance
General Obligations Bonds	\$11,594,000	\$0	\$713,000	\$10,881,000

General Obligation Bonds:

Description	Balance 06-30-10	Due within One Year
Bonds Series 2002 \$525,000 payable in annual installments of \$5,000 to \$20,000 until 2026; with interest ranging from 2.7% to 5.6%	\$ 215,000	\$ 5,000
Bonds Series 2002 \$2,740,000 payable in annual installments of \$70,000 to \$215,000 until 2026; with interest ranging from 2.7% to 5.6%	2,270,000	75,000
Bonds Series 1997 \$400,000 payable in annual installments of \$20,000 to \$40,000 until 2016; with interest ranging from 1.53%	195,000	25,000
Bonds Series 2004 \$180,000 payable in annual installments of \$25,000 to \$30,000 until 2010; with interest ranging from 4.17% to 5%	30,000	30,000
Bonds Series 2004 \$395,000 payable in annual installments of \$55,000 to \$65,000 until 2011; with interest ranging from 3.28% to 4.62%	125,000	60,000
Bonds Series 2005 \$259,000 payable in annual installments of \$35,000 to \$42,000 until 2013; with interest of 4.5% to 7.81%	121,000	39,000
SUB TOTAL	\$ 2,956,000	\$ 234,000

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

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

General Obligation Bonds: (Continuation)

Description	Balance 06-30-10	Due within One Year
Bonds Series 2006 \$975,000 payable in annual installments of \$115,000 to \$170,000 until 2013; with interest of 1.53% to 7.5%	\$ 447,000	\$ 140,000
Bonds Series 2007 \$410,000 payable in annual installments of \$5,000 to \$10,000 until 2031; with interest of 1.53% to 7.5%	395,000	5,000
Bonds Series 2007 \$100,000 payable in annual installments of \$5,000 to \$10,000 until 2021; with interest of 1.53% to 7.5%	85,000	5,000
Bonds Series 2008 \$375,000 payable in annual installments of \$5,000 to \$30,000 until 2032; with interest of 1.53% to 7.5%	370,000	5,000
Bonds Series 2008 \$464,000 payable in annual installments of \$33,000 to \$62,000 until 2018; with interest of 1.53% to 7.5%	428,000	36,000
Bonds Series 2008 \$4,850,000 payable in annual installments of \$70,000 to \$4,340,000 until 2015; with interest of 1.53 to 5.4%	4,780,000	75,000
Bonds Series 2009 \$705,000 payable in annual installments of \$80,000 to \$425,000 until 2016; with interest of 4.75% to 7.5%	625,000	80,000
Bonds Series 2009 \$895,000 payable in annual installments of \$100,000 to \$160,000 until 2016; with interest of 4.75% to 7.5%	795,000	100,000
SUB TOTAL	7,925,000	446,000
TOTAL	\$ 10,881,000	\$ 680,000

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

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

The annual debt requirements for the bonded debt outstanding as June 30, 2010 are as follows:

Year Ending	Principal	Interest	Total
2011	\$ 680,000	\$ 394,037	\$ 1,074,037
2012	703,000	654,681	1,357,681
2013	688,000	634,712	1,322,712
2014	689,000	587,701	1,276,701
2015	552,000	545,942	1,097,942
Subsequent years	7,569,000	4,744,905	12,313,905
TOTAL	\$ 10,881,000	\$ 7,561,978	\$ 18,442,978

The Municipality is required to limit the amount of general obligation debt to 10% of the total assessment of property located within the Municipality, for bonds to be repaid with the proceeds of property tax restricted for debt services. Other obligations include compensated absences, LIMS refinance debt, claims and judgments.

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	\$ 461,459
General funds	526,555
Municipal sales tax	344,827
TOTAL	\$ 1,332,841

Expenditures for the year 2009-2010 were as follows:

Principal	\$ 713,000
Interest	413,695
TOTAL	\$ 1,126,695

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

12. RETIREMENT PLAN

Plan Description

Regular employees of the Municipality contribute to a cost sharing multiple-employer defined benefit retirement plan, administered by the Employee' Retirement System of the Government of Puerto Rico and its instrumentalities (ERS). ERS covers all regular full time public employees working for the central government, public corporations and the municipalities of Puerto Rico. The system provides retirements pensions, death and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Benefits vest after ten years of plan participation. The system was created under Act 447, approved on May 15, 1951, "Retirement Pensions, Disability and Death Benefits", 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 (LAW 447)

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

Participants 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.

No benefit is payable if the participant receives a refund of his accumulated contributions.

Additional information of ERS is provided in its financial statements for the year ended June 30, 2010 a copy of which can be obtained from the ERS, Minillas Station, PO Box 42003, San Juan, PR 00940.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

12. RETIREMENT PLAN (Continuation)

NEW PLAN (REFORMA 2000)

Eligibility

Pension Benefits

Age 65 with 10 years
of service

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

For both plans, the employees are vested when attaining ten years of plan participation. 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.

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

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.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

12. RETIREMENT PLAN (Continuation)

Contribution Requirements

The Municipality's total payroll for the fiscal year 2010 amounted to approximately \$6,675,539. Common wealth legislation requires employees to contribute 5.775% of gross salaries up to \$6,600 plus 8.275% of the gross salary in excess of \$6,600. Municipality is required to contribute 9.275% of gross salary annually during year 2009. Municipality is required and actual contribution under Act 447 and Reforma 2000 were \$154,197 and \$238,196 respectively.

Actuarial Valuation

As of June 30, 2009, the ERS has an unfunded accrual liability of approximately \$17.1 billion, representing a 9.7% funding ratio. This information is not available by each participating government agency or municipalities.

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	7.5% a year
b) Salary increases	3.0% year
c) Pre-retirement Mortality	For General Employees and Mayors, RP-2000 Employee Mortality Rates for males and females projected on a generational basis using Scale AA. For members covered under Act 127, RP-2000 Employee Mortality Rates with blue collar adjustments for males and females, projected on a generational basis using Scale AA.
Post-retirement Health Mortality	Gender-specific mortality rates were developed based on a study of plan's experience from 2003 to 2007. Sample rates shown below are as of 2005 and are thereafter projected on a generational basis using Scale AA.
Post-retirement Disabled Mortality	RP 2000 Disabled Annuitant Mortality Rates, without projection.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

12. RETIREMENT PLAN (Continuation)

Actuarial Valuation (Continued)

d) Termination

Withdrawal rates vary by employee category.

e) Disability

Rates are based on the six month elimination period rates in the 1987 Commissioners Group Disability Table, adjusted as set forth in the table below. Rates of disability cease to apply once a member is eligible for the 75% of the Highest Salary maximum benefit.

Adjustment to 1987 CGDT		
Act	Members Covered under Act 127	Other Members
447	100%	75%
1	100%	75%
2000	<p>100% if more than 10 years from retirement eligibility.</p> <p>300% if at or past retirement eligibility.</p> <p>Interpolated from 100% to 300% in the 10 years leading up to retirement eligibility.</p>	75%

100% of disabilities occurring while in active service are assumed to be occupational for members covered under Act 127. For other members, 90% of disabilities occurring while in active service are assumed to be occupational and 10% are assumed to be non-occupational.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

12. RETIREMENT PLAN (Continuation)

Actuarial Valuation (Continued)

f) Retirement

Rates of retirement vary by employment category, Act, and by age and years of Creditable Service.

Act 447 General Employees (Includes General Hazardous Employees)			
	Service Condition		
Age	10 years	25 years	30 years
45 to 49			10.0%
50 to 53			15.0
54			20.0
55 to 57		10.0%	20.0
58	5.0%	10.0	20.0
59 to 64	10.0	15.0	20.0
65 to 69	15.0	15.0	20.0
70	100.0	100.0	100.0

System 2000 General Employees		
Age	Non-hazardous	Hazardous
60 to 66	15.0%	12.0%
67	100.0	100.0

Act 447 Police & Fire			
	Service Condition		
Age	10 years	25 years	30 years
45 to 48			10.0%
49			15.0
50		7.0%	15.0
51 to 56		15.0	20.0
57		20.0	30.0
58	2.5%	20.0	100.0
59 to 64	10.0	25.0	
65 to 69	10.0	30.0	
70	100.0	100.0	

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

12. RETIREMENT PLAN (Continuation)

Actuarial Valuation (Continued)

System 2000 Police & Fire			
Age	Service Condition		
	10 years	25 years	30 years
45 to 48			9.0%
49			13.5
50		6.3%	13.5
51 to 56		13.5	18.0
57		18.0	27.0
58	2.25%	18.0	27.0
59 to 64	9.0	22.5	27.0
65 to 69	9.0	27.0	31.5
70	100.0	100.0	100.0

- g) Proportion of participants with spouses 50% of participants assumed to be married at retirement, with females assumed to be four years younger than males.
- 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

Accordingly, the pension expense for fiscal year 2010 was approximately \$392,393 that represented 100% of the contributions required by funding policies of the Plan.

13. LONG TERM LIABILITIES

Compensated Absences

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, 2010 are as follows:

Governmental activity	June 30, 2009	Net decrease	June 30, 2010	Due within One year
Compensated Absences	\$ 1,111,257	\$ 174,971	\$936,286	\$ 222,130

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

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 expenditures for the year ended June 30, 2010, were approximately \$ 75,197 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.

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.

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 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 operations by the Comptroller's Office.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

16. MUNICIPAL SALES TAX

Pursuant to the provisions of the Law number 80 of July 29, 2007 and effective August 1, 2007, the citizenship contribution was uniformly established in 1.5% of which 1% will be collected by the Municipalities and the remaining .5% will be collected by the Treasury Department of the Commonwealth of Puerto Rico. Also, this Law uniformed the use of the contribution of 1.5% in the following activities: solid waste disposal costs, recycle, public works and improvements, health services and security services.

The Municipalities of Puerto Rico are responsible to collect 1% of the corresponding tax with the same exemptions and limitations that the portion collected by Treasury Department. The Act provides and optional surtax on the un-processed food. This surtax must be approved by the Municipal Legislature. The Treasury Department is responsible to create the Municipal Development Fund (.02%), the Municipal Redemption Fund (.02%) and the Municipal Improvements Fund (.01%) with the remaining 0.5%. The Municipality collected \$619,037 during the year ended June 30, 2010.

17. CONTINGENCIES, LIABILITIES FOR CLAIMS AND JUDGMENTS AND OTHER

Contingencies and claims and judgments against the Municipality

The **Municipality** is a defendant in a number of lawsuits arising principally from claims against the **Municipality** for alleged improper actions. It is management's opinion, based on the advise of the legal counsel, that the probable claims against the **Municipality** not covered by insurance are by the amount of \$73,928 at June 30, 2010, the financial condition of the **Municipality** adjusted for that amount.

MUNICIPALITY OF PATILLAS, PUERTO RICO
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

18. RESTATEMENT OF 2009 FINANCIAL STATEMENTS

During the fiscal year ended June 30, 2010 **the Municipality** notes that certain liabilities had been overstated or understated as well as other differences related with adjustments to capital assets and reclassification of certain fund balances. As a result the net assets at June 30, 2009, as previously reported, had been increased by \$3,161,629 and the fund balance of various funds at June 30, 2009, as previously reported, had been increased by \$400,234 the debt service fund, increased by \$133,205 the Bond issued fund, increased HUD programs by \$34,485, increased Homeland Security Program by \$485,710, decreased general fund by \$62,420 and other funds decrease by \$201,793.

	<u>Net Assets</u>	<u>General Fund</u>	<u>Hud Program</u>	<u>Hom eland Security Programs</u>	<u>Bond issued fund</u>	<u>Debt Service</u>	<u>Other Funds</u>
Beginning balance at June 30, 2009	\$ 13,059,386	\$ 39,188	\$ 45,802	\$ -	\$ 7,594,883	\$ 162,114	\$ 348,598
Accounts payable from prior year cancelled	-	-	34,485	485,710	133,205	400,234	-
Accounts payable from prior year	(3,161,629)	(62,420)	-	-	-	-	(201,793)
Beginning balance, as restated June 30, 2009	<u>\$ 9,897,757</u>	<u>\$ (23,232)</u>	<u>\$ 80,287</u>	<u>\$ 485,710</u>	<u>\$ 7,728,088</u>	<u>\$ 562,348</u>	<u>\$ 146,805</u>

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

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

I have audited the financial statements of the governmental activities of Municipality of Patillas, Puerto Rico as of and for the year ended June 30, 2010 and have issued my report thereon dated December 17, 2010 which was unqualified. 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.

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 integral control over financial reporting as item 2010-02 and 2010-03.

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 in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, I believe that none of the significant deficiencies described above is a material weakness.

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 our tests disclosed instances of no compliance 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 2010-04.

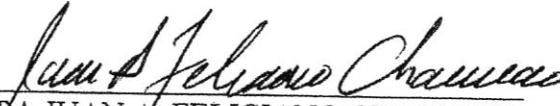
I noted certain matters that I reported to management of Municipality of Patillas, Puerto Rico in a separate letter dated December 17, 2010.

Municipality of Patillas, Puerto Rico's response to the finding identified in my audit is 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.

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
December 17, 2010

The stamp number 2541929
was affixed to the
original of this report


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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, 2010. 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, Local Governments and Non-Profit Organizations". Those standards and OMB Circular A-133 require that I plan and perform the audit to obtain reasonable assurance about whether 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's 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 of Municipality of Patillas's compliance with those requirements.

As described in the findings 2010-04 and 2010-05, the accompanying schedule of findings and questioned costs, Municipality of Patillas did not comply with the requirements regarding reporting and cash management applicable to its Disaster Grant Public Assistance and Section 8 Housing Choice Voucher. Compliance with such requirements is necessary, in my opinion, for the Municipality of Patillas, to comply with the requirements applicable to that program.

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, 2010. The results of my auditing procedures also disclosed other 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 2010-02.

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 internal control over compliance. Accordingly, I do not express an opinion on the effectiveness of Municipality of Patillas, Puerto Rico's internal control over compliance.

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

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. I consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 2010-02 to be significant deficiencies.

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. Of the significant deficiency in internal control over compliance described in the accompanying schedule of findings and questions costs, I consider item 2010-02 to be material weakness.

Municipality of Patillas, Puerto Rico's 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
December 17, 2010

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CPA JUAN A. FELICIANO CHARNECO
License No. 1263
Expires December 1, 2013

MUNICIPALITY OF PATILLAS, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

Federal Grantor / Pass-through Grantor Program Title	Federal CFDA Number	Pass-through Grantors Number	Federal Expenditures
<u>U.S. Department of Housing and Urban Development</u>			
<u>Direct Program:</u>			
Department of Housing and Urban Development Public and Indian Housing Section 8 - Housing Choice Voucher	14.871	RQ46-EO-57-001/002	\$ 319,279 <u>319,279</u>
<u>Direct Program:</u>			
ARRA - Homeless Prevention & Rapid Re-housing Program	14.257	N/A	<u>9,002</u> 9,002
Passed-through Commonwealth of Puerto Rico			
Commissioners Office of Municipal Affairs			
Community Planning and Development			
Community Development Block Grant (State Program)	14.228	FC-2009	9,202
	14.228	AB-2009	53,247
	14.228	FC-2008	280,562
	14.228	AB-2008	161,450
	14.228	FRP-2007	14,041
	14.228	FC-2007	39,755
	14.228	AB-2007	33,707
	14.228	FC-2006	121,459
	14.228	AB-2006	43,631
	14.228	AC-2005	157,872
	14.228	DR-2005	13,061
	14.228	HP-2004	22,705
	14.228	FC-2004	23,971
	14.228	FC-2002	<u>4,500</u>
			<u>979,163</u>
Passed-through Commonwealth of Puerto Rico Governors Offices			
Municipal Affairs			
ARRA - Community Development Block Grant Program ARRA Entitlement Grant	14.253	N/A	<u>132,078</u>
<u>Total U.S. Department of Housing and Urban Development</u>			<u>1,439,522</u>
<u>U.S. Department of Health and Human Services:</u>			
<u>Direct Program:</u>			
Head Start	93.600	02CH9911/05	826,569
<u>Direct Program:</u>			
ARRA Head Start	93.708	02SE9911/01	39,590
Passed-through Commonwealth of Puerto Rico Governors Office for the Care and Integral Development of Children:			
Department of the Families of Puerto Rico			
Child Care Mandatory Matching Fund of the Child Care and Development Fund	93.596	G0703PRCCDF	<u>48,861</u>
<u>Total U.S. Department of Health and Human Services</u>			<u>915,020</u>

See notes to the schedule of expenditures of federal awards.

MUNICIPALITY OF PATILLAS, PUERTO RICO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2010

Federal Grantor / Pass-through Grantor Program Title	Federal CFDA Number	Pass-through Grantors Number	Federal Expenditures
<u>U.S. Department of Agriculture</u>			
Passed-through Commonwealth of Puerto Rico Governors Office			
Department of Education of Puerto Rico			
Child and Adult Care Food Program	10.558	PI-HS-06-02(CCC-198)	67,551
Total U.S. Department of Agriculture			67,551
 <u>U.S. Department of Homeland Security</u>			
Public Assistance Grant			
Passed-through Commonwealth of Puerto Rico Governors Office			
Authorized Respresentative to FEMA (GAR)			
Disaster Grant Public Asistance - Lluvias noviembre 2003	97.036	N/A	5
Disaster Grant Public Asistance - Tormenta George	97.036	N/A	300
Disaster Grant Public Asistance - Lluvia noviembre 2005	97.036	N/A	270,129
Disaster Grant Public Asistance- Lluvias septiembre 2008	97.036	FEMA DR-PR1798	728,512
Total U.S. Department of Homeland Security			998,946
 <u>U.S Department of Transportation Federal Transit Administration</u>			
Passed-through Commonwealth of Puerto Rico Governors Offices			
Department of Transportation and Public Works of P.R.			
Federal Transit - Capital Investment Act	20.500	N/A	91,252
Total U.S Department of Transportation			91,252
 <u>U.S Department of Energy</u>			
Passed-through Commonwealth of Puerto Rico Governors Offices			
Energy Affairs Administration			
ARRA- Energy Efficiency and Conervation Block Grant Program	81.128	N/A	10,250
Total U.S Department of Energy			10,250
TOTAL FEDERAL ASSISTANCE			\$ 3,522,541

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, 2010

(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, Health and Human Services Programs, Homeland Security Programs and **American Recovery and Reinvestment Act Program** represent the major federal financial awards of the Municipality. Major federal awards represent 94% 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:

<u>Description</u>	<u>Hud Programs</u>	<u>Head Start Programs</u>	<u>Homeland Security Programs</u>	<u>Other funds</u>	<u>Total</u>
Federal Programs Expenditures	\$ 1,439,522	\$ 915,020	\$ 998,946	\$ 169,053	\$ 3,522,541
State & Municipal Expenditures				132,673	\$ 132,673
TOTAL	\$ 1,439,522	\$ 915,020	\$ 998,946	\$ 301,726	\$ 3,655,214

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010**

A. Summary of Audit results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness (es) identified? Yes No

Significant deficiency (s) identified not considered
to be material weaknesses? Yes No
None reported

Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over major programs:

Material weakness (es) identified? Yes No

Significant deficiency (s) identified not
Considered being material weaknesses? Yes No

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

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

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010**

Identification of Major Programs

CFDA Number(s)	Name of Federal Program or Cluster
14.228	Community Development Grant (State Program)
14.871	Section 8 Housing Choice Voucher
14.253	ARRA - Community Development Block Grant Program ARRA Entitlement Grant
93.600	Head Start
97.036	Disaster Grant - Public Assistance
14.257	ARRA - Homeless Prevention & Rapid Re-housing Program
81.128	ARRA - Energy Efficiency and Conservation Block Grant Program
93.708	ARRA - Head Start

Dollar threshold used to distinguish
Between type A and type B Programs

\$300,000

Auditee qualified as low-risk audit

___ Yes X No

B – Federal Award Findings and Questioned Cost

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010
(continued)**

**Program: Accounting and Finance Department
General Fund
Year ended June 30, 2010**

Ref. No. -----	Finding / Noncompliance -----	Questioned Cost -----
2010-01	<p><u>Statement of Condition and Criteria</u></p> <p>The Municipality is operating by a decrease in revenues during the year accordingly by the criteria established by the Standards of Financial Management Systems for Regulations for Municipal Administration; and with GASB codifications 1700, with requirements stated in OMB Circular A-133.</p> <p><u>Cause</u></p> <p>The Municipality has significant deficiencies in its accounting and financial management systems and financial reporting practices caused by the government operations as related to budgets for the General Fund.</p> <p><u>Effect</u></p> <p>The lack of budget may affect the Municipality results :</p> <ul style="list-style-type: none"> a) To provide services to citizens without affecting them. b) To determine compliance with finance – related legal and contractual provisions. <p><u>Auditors Recommendation</u></p> <p>The Municipality should revised and evaluate in a monthly basis revenues and disbursements to adjust disbursements to the revenues receipt to comply with Budget requirements of Municipal Law number 81 of August 30, 1991 as amended. Evaluate the impact in the revenues of the change in construction tax and the increase of the real and personal taxes.</p> <p><u>Municipality Response</u></p> <p>The Municipality will evaluate the actual administrative procedures being followed. The Municipality management took serious and radical measure to minimize the impact of this condition and expect to correct in the near future. Revenues budget were reduced by the Puerto Rico economic conditions, several disaster events affected directly the Municipality and we continues the services needed by the citizens using the operational funds.</p>	-0-

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010
(continued)**

**American Recovery and Reinvestment Act
CFDA No. 14.257
Grant No. Homeless Prevention & Rapid Re-Housing Program
Year ended June 30, 2010**

Ref. No.	Finding / Noncompliance	Questioned Cost
-----	-----	-----
2010-02	<p><u>Statement of Condition and Criteria</u></p> <p>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.</p> <p><u>Cause</u></p> <p>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).</p> <p><u>Effect</u></p> <p>The Municipality did not maintain adequate procedures for the Administration of cash because the instructions for the use of funds were not available.</p> <p><u>Auditor's Recommendation</u></p> <p>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.</p> <p><u>Municipality Response:</u></p> <p>The Municipality evaluates the actual administrative procedures. The Mayor gave instructions to implement immediately.</p>	-0-

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010
(continued)**

**Department of Homeland Security
CFDA No. 97.036
Grant No. Disaster Grant Public Assistance
Year ended June 30, 2010**

Ref. No.	Finding / Noncompliance	Questioned Cost
-----	-----	-----
2010-03	<p><u>Statement of Condition and Criteria</u></p> <p>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 Governor's Office Authorized Representative to FEMA (GAR) 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.</p> <p><u>Cause</u></p> <p>The Municipality did not comply with the Cash Management Requirements of the Department of Treasury of the United States as per Title 44 of CFR, part 13.20 (cc) (7).</p> <p><u>Effect</u></p> <p>The Municipality did not maintain adequate procedures for the Administration of cash.</p> <p><u>Auditor's Recommendation</u></p> <p>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.</p> <p><u>Municipality Response:</u></p> <p>The Municipality evaluates the actual administrative procedures. The Mayor gave instructions to implement immediately.</p>	-0-

**MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010
(continued)**

**U. S. Department of Homeland Security
CFDA No. 97.036
Grant No. Disaster Grant Public Assistance
Year ended June 30, 2010**

Ref. No.	Finding / Noncompliance	Questioned Cost
2010-04	<u>Statement of Condition and Criteria</u> <u>Accounting and Cash Management</u>	-0-

It was noted in my test of compliance that the Municipality is not complying with the criteria established by the Standards of Financial management Systems, in 44CFR Part 13, Sub-Part C, Section 13.20, Uniform Administrative Requirements, were is established that management system shall provide for the following:

1. Accurate, current and complete disclosure of the financial results of each federally sponsored project or program in accordance with the reporting requirements.
2. Records that identify adequately the source and application of funds for federally sponsored activities. These records shall contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, income and interest.

To established procedures to comply with Financial and Program Management Standards of funds of the Disaster Grant Public Assistance Program. It was noted during my audit that Municipality does not maintain proper segregated accounting records general ledger, check register, Trial balance, Budget comparison by program years.

Cause

The Municipality does not comply with the Financial and Program Management System Standards. The municipality does not maintained a General Ledger by year grant to properly segregate fund by grant, do not prepare accurate trial balance in a monthly basis.

Effect

The Municipality does not maintain adequate accounting procedure that segregates accounting rewards by program year for the Administration of funds from Disaster Grant Public Assistance Program by grant funds.

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010
(continued)

Auditors Recommendation

The Municipality must establish adequate procedures in order to control in a more effective manner the financial and Program Management System Standards.

Municipality Response:

The Municipality will review the auditor recommendation and the Mayor grave instructions to implement immediately.

**MUNICIPALITY OF PATILLAS
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 FOR THE YEAR ENDED JUNE 30, 2010
 (continued)**

**U. S. Department of Housing and Urban Development
 CFDA No. 14.871
 Grant No. Section 8 Housing Choice Voucher
 Year ended June 30, 2010**

Ref. No.	Finding / Noncompliance	Questioned Cost
2010-05	<u>Statement of Condition and Criteria</u> <u>Accounting and Cash Management</u>	-0-

It was noted in my test of compliance that the Municipality is not complying with the criteria established by the Standards of Financial management Systems, in 24CFR Part 84, Sub-Part C, Section 7, Uniform Administrative Requirements, where it is established that management system shall provide for the following:

1. Accurate, current and complete disclosure of the financial results of each federally sponsored project or program in accordance with the reporting requirements.
2. Records that identify adequately the source and application of funds for federally sponsored activities. These records shall contain information pertaining to Federal awards, authorizations, obligations, unobligated balances, assets, outlays, income and interest.

To establish procedures to comply with Financial and Program Management Standards of funds of the Section 8 Housing Choice Voucher Program. It was noted during my audit that Municipality does not maintain proper segregated accounting records general ledger, Trial balance, Budget for the program.

Cause

The Municipality does not comply with the Financial and Program Management System Standards. The municipality does not maintain a Program General Ledger and do not prepare accurate trial balance in a monthly basis.

Effect

The Municipality does not maintain adequate accounting records for the Administration of funds from Section 8 Housing Choice Voucher Program by grant funds.

MUNICIPALITY OF PATILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010
(continued)

Auditors Recommendation

The Municipality must establish adequate procedures in order to control in a more effective manner the financial and Program Management System Standards.

Municipality Response:

The Municipality will review the auditor recommendation and the Mayor gave instructions to implement immediately.

**MUNICIPALITY OF PATILLAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2010**

2009 – Finding No. 1: U.S. Department of Housing and Urban Development
Public and Indian Housing
Section 8 – Voucher
CFDA No. 14.871
Year ended June 30, 2009
Finding was corrected.

2009 – Finding No. 2: U.S. Department of Housing and Urban Development
Public and Indian Housing
Section 8 – Voucher
CFDA No. 14.871
Year ended June 30, 2009
Finding reported again.

**CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2010**

Ref. No. 2010-01	<u>Finding /Corrective Action</u> <u>Planned/Person Responsible:</u> <u>Statement of Condition:</u> The General Fund is not complying with budget balances and criteria established by the Standards of Financial Management System for Regulations for Municipal Administration, with GASB codification 1700, with requirements stated in OMB Circular A-133 and with Budget requirements of Municipal Law number 81 of August 30, 1991 as amended. <u>Corrective Action Planned:</u> The Finance Director will establish adequate procedure to permit the preparation of reliable budget and comply with all standards, requirements and laws that apply. <u>Person Responsible:</u> Mr. Luis Acevedo Finance Director	<u>Anticipated Completion Date</u> On or before end of 2010-11 fiscal year
Ref. No. 2010-02	<u>Finding /Corrective Action</u> <u>Homeless Prevention – Stimulus Program:</u> <u>Statement of Condition:</u> The Homeless Prevention Reinvestment Program cash balance over \$5,000 for periods larger than 3 days. <u>Corrective Action Planned:</u> The Homeless Prevention Reinvestment Program Administration will evaluate and implement adequate procedures to control, use and invest in effective manner, federal funds. <u>Person Responsible:</u> Mr. Luis Acevedo Finance Director	<u>Anticipated Completion Date</u> On or before end of 2010-11 Fiscal year



TRAMITE DE CORRESPONDENCIA

Dirigido a:

Fecha: _____

Hora: _____

Oficina del Comisionado

Oficina del Comisionado

Auditora Interna

Asesor Convenio Colectivo

Asesoramiento Legal

Oficial de Comunicaciones

Programa de Justicia Juvenil

Comisionados Auxiliares

Programas Federales

Sistemas de Información

Código Orden Público

FEM

Area de Asesoramiento,
Reglamentación e Int. Fiscal

Organizaciones Comunitarias

Hogar Propio

Administración (Para uso de la Oficina de Administración)

Recursos Humanos

Servicios Generales

Informática

Finanzas

Presupuesto/Planificación

TRÁMITE:

Contestar

Informar

Discutir

Firmar

Revisar

Aprobar

Acción Pertinente

Asunto: _____

J. P. Torres
Single Audit

**CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2010**

Ref. No.	<u>Finding /Corrective Action</u>	<u>Anticipated</u>
2010-03	<u>Disaster Grant Public Assistance:</u>	<u>Completion Date</u>

Statement of Condition:

The Disaster Grant Public Assistance program cash balance over \$5,000 for periods larger than 3 days.

On or before
end of 2010-11
Fiscal year

Corrective Action Planned:

The Disaster Grant Public Assistance program Administration will evaluate and implement adequate procedures to control, use and invest in effective manner, federal funds.

Person Responsible:

Mr. Luis Acevedo
Finance Director

Ref. No.	<u>Finding /Corrective Action</u>	<u>Anticipated</u>
2010-04	<u>Planned/Person Responsible:</u>	<u>Completion Date</u>

Statement of Condition:

The financial accounting for each federally sponsored project or program will be in accordance with the reporting requirements.

On or before
end of 2009-10
fiscal year

Corrective Action Planned:

The Finance Director will establish adequate procedure to permit the preparation of reliable budget and comply with all standards, requirements and laws that apply. The Mayor gave instruction to implement the financial reporting requirements as soon as possible.

Person Responsible:

Mr. Luis Acevedo
Finance Director

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

Sr. Luis Acevedo
Finance Director

**CORRECTIVE ACTION PLAN
YEAR ENDED JUNE 30, 2010**

Ref. No. Finding /Corrective Action
2010-05 Planned/Person Responsible:

Anticipated
Completion Date

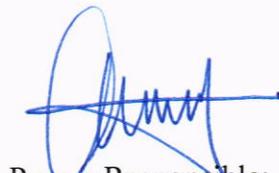
Statement of Condition:

The financial accounting for each federally sponsored project or program will be in accordance with the reporting requirements.

On or before
end of 2009-10
fiscal year

Corrective Action Planned:

The Finance Director will establish adequate procedure to permit the preparation of reliable budget and comply with all standards, requirements and laws that apply. The Mayor gave instruction to implement the financial reporting requirements as soon as possible.



Person Responsible:
Mr. Luis Acevedo
Finance Director