
COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PATILLAS

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

YEAR ENDED JUNE 30, 2014



Municipality of Patillas
P.O. Box 698 Patillas, P.R. 00723
Hon. Norberto Soto Figueroa

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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

INDEPENDENT AUDITORS' REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of the **Municipality of Patillas, Puerto Rico (the Municipality)**, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the **Municipality's** basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the discretely presented component unit. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the discretely presented component unit is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessment, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our modified audit opinions.

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Basis for Adverse Opinion on the Government-Wide Financial Statements – Statement of Net Position and Statement of Activities

The Municipality has not maintained complete and adequate records in order to obtain sufficient and competent evidential matter of the capital assets, accumulated depreciation and net capital assets, are recorded in the accompanying statement of net position at June 30, 2014 stated at \$40,528,482, (\$10,108,265) and \$31,303,662.

Management has not capitalized certain acquisitions of property and equipment and the construction in progress in the governmental activities and, accordingly, such disbursements are recognized as expenses in the fiscal year 2014. Accounting principles generally accepted in the United States of America require that those assets be capitalized and depreciated, which would increase the assets, net position and expenses of the governmental activities.

Adverse Opinion – Government – Wide Financial Statements

In our opinion, because of the significance of the matters discussed in the of Basis for Adverse Opinion on Governmental Activities” paragraph, the financial statement referred to above do not present fairly the financial position of the governmental activities” paragraph, the financial statements referred to above do not present fairly the financial position of the governmental activities of the **Municipality of Patillas**, Puerto Rico, as of June 30, 2014, as to whether they have been properly prepared, in all material respects in accordance with accounting principles generally accepted in the United State of America.

Basis for Qualified Opinion on the Governmental Funds Financial Statement

The Municipality did not maintain adequate accounting records of the interfund cash transactions and the corresponding due from and due to account balances. We were unable to obtain sufficient evidence to support and satisfy ourselves about the amounts recorded as interfund due to/due from in total the amount of \$5,170,949 reported in the Balance Sheet of the governmental funds at June 30, 2014.

Qualified Opinion – Governmental Funds

In our opinion, except for the possible effects of the matter discussed in the “Basis for Qualified Opinion on Government Funds” paragraph, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2014, and the respective changes in financial position thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.



López-Vega, CPA, PSC

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INDEPENDENT AUDITORS' REPORT (CONTINUED)

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages **5** through **14** and **56** be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because of the limited - procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the **Municipality of Patillas'** basic financial statements. The accompanying supplementary information – Schedule of Expenditures of Federal Awards shown in page **58** 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 also not a required part of the basic financial statements.

The Schedule of Expenditures of Federal Awards is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 26, 2015, on our consideration of the **Municipality's** internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters.



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Other Reporting Required by Government Auditing Standards (continued)

The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the **Municipality's** internal control over financial reporting and compliance.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
June 26, 2015

Stamp No. 2675847 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



This 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 on June 30, 2014. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. This document also includes comparative data with prior year as this information was available for the fiscal year ended on June 30, 2013. This MD&A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

1. a broader basis in focusing important issues;
2. acknowledgement of an overview of the Municipality's financial activities;
3. an evaluation of its financial condition as of the end of fiscal year 2013-14 compared with prior year results;
4. identification of uses of funds in the financing of the Municipality's variety of activities; and
5. a basis to assess management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

The financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2014 constitute factual evidence of the Municipality's economic situation by the end of such year. The following comments deserve special mention:

1. Total assets of the Municipality as of the end of fiscal year 2013-2014 amounted to \$38,871,963 which represents an increase of 4% compared to prior fiscal year, as restated.
2. At the end of fiscal year 2014, total liabilities amounted to \$24,227,735. Out of said amount, \$21,160,992 corresponded to long-term liabilities of which \$15,195,000 represented the outstanding balance of bonds and notes issued. The Municipality continued to meet all debt service requirements, most of which was paid from self-generated revenues.
3. Total net position of the Municipality as of the end of fiscal year 2013-2014 amounted to \$14,644,228 which represents an increase of 11% compared to prior fiscal year, as restated.
4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$15,013,425 derived from the following sources: \$51,886 from charges for services; \$1,256,285 from operating grants and contributions; \$2,852,305 from capital grants and contributions obtained from other sources, and \$10,852,949 from general revenues available.

FINANCIAL HIGHLIGHTS (CONTINUED)

5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$13,558,361.
6. As reflected in the Statement of Activities, the current fiscal year operations contributed to an increase in the Net Position figure by \$1,455,064.
7. As of the close of the current fiscal year, the Municipality's Governmental Funds reported combined ending fund balances of \$4,015,814.
8. As the end of the current fiscal year, the Municipality's general fund balance reflects a deficit of \$5,585,613, compared to a fund deficit of \$7,727,477 in the prior fiscal year. After the reclassification debt, (Consolidate Waste Debt Agreement, Puerto Rico Aqueduct and Sewer Authority - Debt Agreement and others.) from Fund Financial to Governmental Wide; the beginning fund deficit was 5,585,613.
9. The actual General Fund budgetary activities resulted in an unfavorable balance of (\$485,210).

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2014. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

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

FINANCIAL STATEMENTS COMPONENTS

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

The Statement of Net Position reflects information of the Municipality as a whole on a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year.

USING THIS ANNUAL REPORT

This annual report consists of a series of new financial statements with a change in the focus from previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

GOVERNMENT – WIDE FINANCIAL STATEMENTS

The Government-Wide Financial Statements are designed to provide users of the financial statements with a broad overview of the Municipality's finances in a manner similar to private-sector companies.

The Statement of Net Position presents information on all of the Municipality's assets and liabilities, with the difference between both reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the Statement of Activities that will only result in cash flows in future fiscal periods. The Statement of Activities is focused on both the gross and net cost of various activities, which are provided by the government's general tax and other revenues. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

FUND FINANCIAL STATEMENTS

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government-Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements, focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

FUND FINANCIAL STATEMENTS (CONTINUED)

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the Municipality's near term financial decisions. Both of the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

INFRASTRUCTURE ASSETS

Historically, a government's largest group of assets (infrastructure-roads, bridges, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the Governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach) which periodically (at least every third year), by category, measures and demonstrated its maintenance of locally established levels of service 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 statement users in evaluating a local government and its performance over time.

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

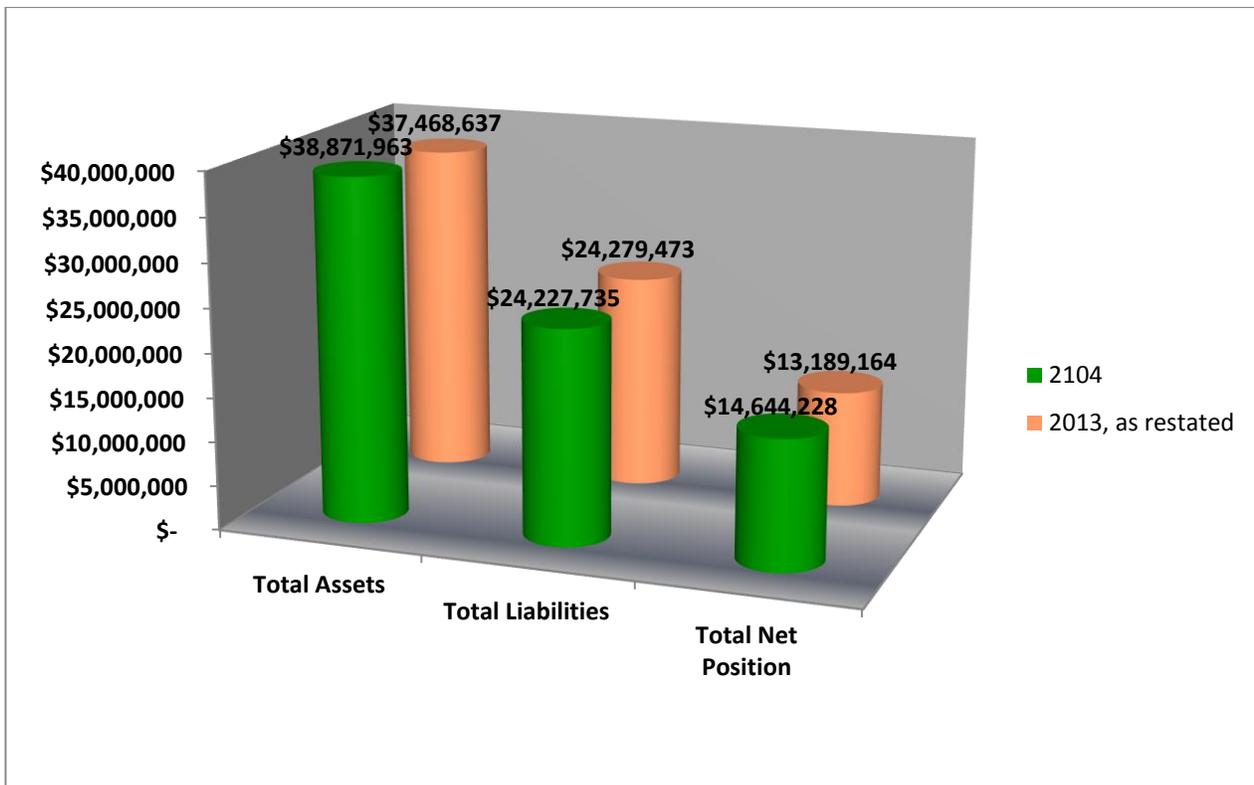
FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Position

The Statement of Net Position serves as an important indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Patillas, primary government assets exceeded total liabilities by \$14,644,228 at the end of 2014, as compared with \$13,189,164, which reflect an increase of \$1,455,064 when compared with previous fiscal year, as restated. The following condensed Statements of Net Position of the Primary Government shows on a comparative basis the most important components of the \$1,455,064 increase reflected in the Net Position figure.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Condensed Statements of Net Position	2014	2013	Change	%
Current and other assets	\$ 7,568,301	\$ 7,254,167	\$ 314,134	4%
Capital assets	31,303,662	30,214,470	1,089,192	4%
Total assets	38,871,963	37,468,637	1,403,326	4%
Current and other liabilities	3,456,743	4,573,480	(1,116,737)	-24%
Long-term liabilities	20,770,992	19,705,993	1,064,999	5%
Total liabilities	24,227,735	24,279,473	(51,738)	.02%
Net investment in capital assets	25,413,662	23,019,469	2,394,193	10%
Restricted	9,601,427	9,436,930	164,497	2%
Unrestricted deficit	(20,370,861)	(19,267,235)	(1,103,626)	6%
Total net position	\$ 14,644,228	\$ 13,189,164	\$ 1,455,064	11%



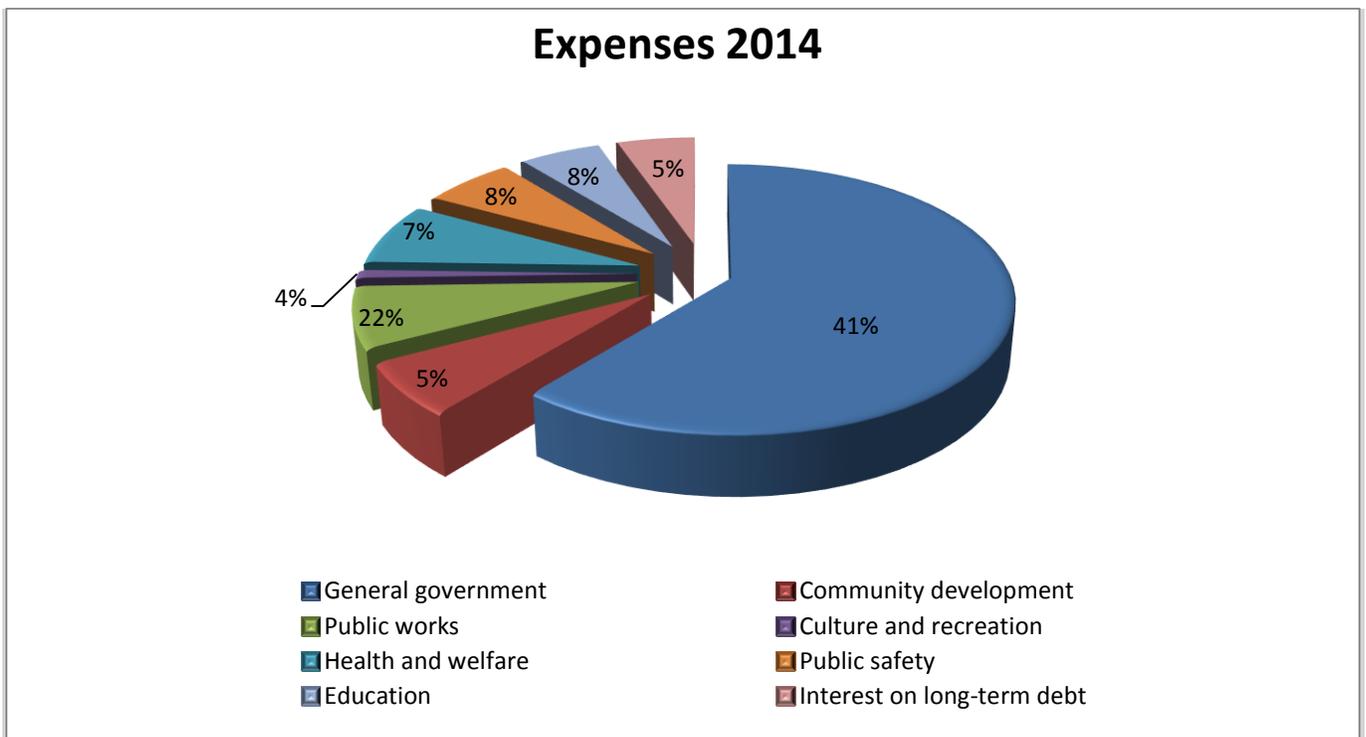
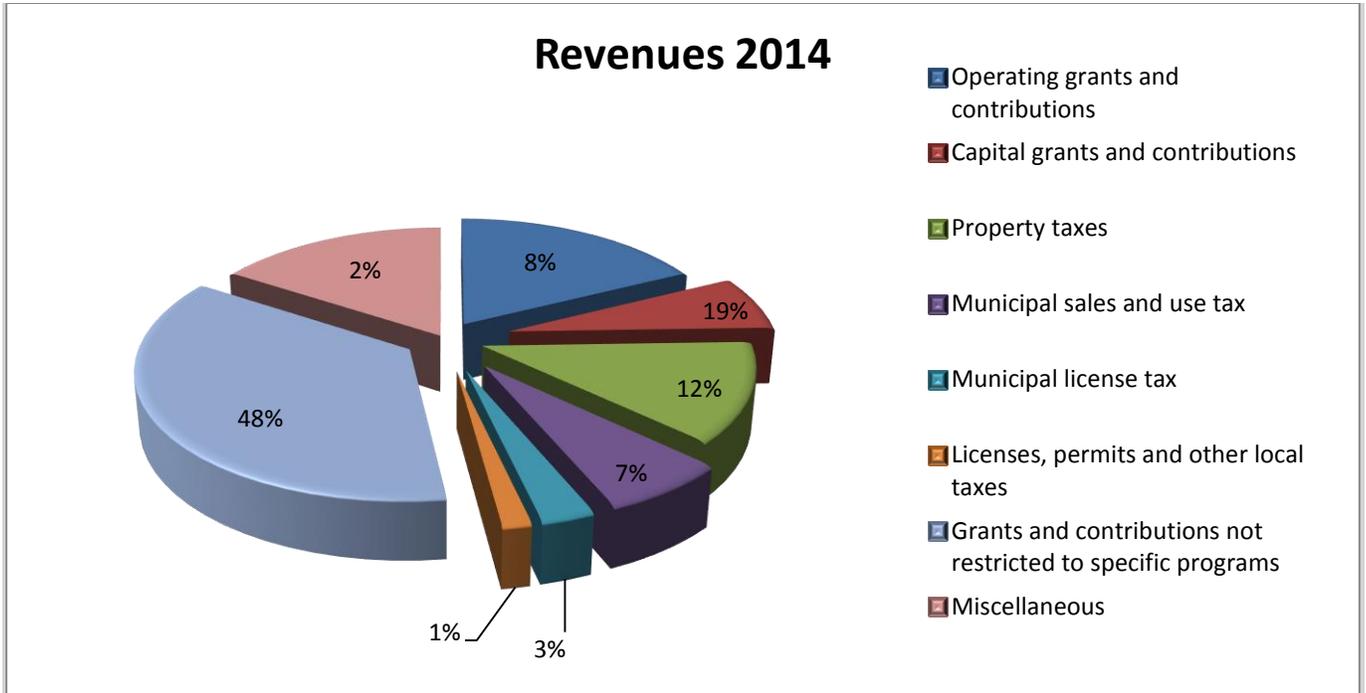
FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Changes in Net Position

The Municipality's net position increased by \$1,455,064. Approximately twenty three percent (23%) of the Municipality's total revenue came from taxes, while seventy-four percent (74%) resulted from grants and contributions, including federal aid. Charges for Services and Interest and Investment earnings provided less than one percent and miscellaneous (2%) of total revenues. The Municipality's largest expenses included items such as general government, health and welfare services, public works, community development and public safety. The following table and graphic presentation includes in absolute and relative terms, the composition of revenues and expenses for the fiscal years ended on June 30, 2013 and 2014. Such analysis helps the reader to evaluate the Municipal administration performance in the administration of its current financial operations.

Condensed Statements of Activities	2014	2013 as restated	Change	%
Program revenues:				
Charges for services	\$ 51,886	\$ 64,298	\$ (12,412)	-19%
Operating grants and contributions	1,256,285	2,812,559	(1,556,274)	-55%
Capital grants and contributions	2,852,305	1,085,607	1,766,698	163%
General revenues:				
Property taxes	1,772,165	1,973,234	(201,069)	-10%
Municipal sales and use tax	1,043,458	1,073,962	(30,504)	-3%
Municipal license tax	477,770	436,939	40,831	9%
Licenses, permits and other local taxes	196,552	236,566	(40,014)	-17%
Grants and contributions not restricted to specific programs	7,018,818	7,656,828	(638,010)	-8%
Interest and investment earnings	4,498	4,970	(472)	-9%
Miscellaneous	339,688	702,627	(362,939)	-52%
Total revenues	<u>15,013,425</u>	<u>16,047,590</u>	<u>(1,034,165)</u>	-6%
Expenses:				
General government	5,554,989	10,898,150	(5,343,161)	-49%
Public safety	1,050,917	1,104,351	(53,434)	-5%
Public works	3,078,861	1,300,516	1,778,345	137%
Culture and recreation	560,640	172,040	388,600	226%
Health and welfare	923,150	1,342,307	(419,157)	-31%
Economic development	-	18,438	(18,438)	-100%
Community development	631,348	1,120,668	(489,320)	-44%
Education	1,086,331	986,970	99,361	10%
Interest on long-term debt	672,125	933,918	(261,793)	-28%
Total expenses	<u>13,558,361</u>	<u>17,877,358</u>	<u>(4,318,997)</u>	-24%
Change in net position	1,455,064	(1,829,768)	3,284,832	-180%
Net position, beginning of year, as restated	13,189,164	15,018,932	(1,829,768)	-12%
Net position, end of year	<u>\$ 14,644,228</u>	<u>\$ 13,189,164</u>	<u>\$ 1,455,064</u>	11%

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

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

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$4,015,814, a decrease of \$291,879 in comparison with the prior year, as restated. The combined fund balances include restricted fund balances amounting to \$9,601,427. This is the portion of fund balance that reflects resources that are subject to externally enforceable legal restrictions 1) to pay for specific program purposes (including capital projects and operational purposes) (\$8,592,741) and; 2) to pay debt services (\$1,008,686). Consequently, since there is an excess of restricted and committed fund balances over total fund balances, a negative unassigned fund balance of (\$5,585,613) was reported in the governmental funds at June 30, 2014.

Governmental funds include the General Fund, which is the main operating fund of the Municipality. As of June 30, 2014, the General Fund has an accumulated deficit of \$5,585,613 compared with prior fiscal year with deficit of \$5,662,693, as restated.

GENERAL FUND BUDGETARY HIGHLIGHTS

During fiscal year 2013-2014, the Municipal Legislature approved revisions to the operational budget that was prepared in accordance to the analysis of previous year's results. Despite of the balance budget, the expected amounts of revenues were not collected, as reflected in exhibit. Budgetary Comparison Schedule-General Fund attached here to. The Municipality of Patillas current year operation had a deficiency of revenues over expenses of (\$485,210).

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2014, amounted to \$41,411,927 which upon deduction of accumulated depreciation in the amount of \$10,108,265 produced a net book value attributable to capital assets in the amount of \$31,303,662. Said investment includes land, construction in progress, buildings, improvements, equipment, infrastructure, furnishing, computers and vehicles. Infrastructure assets are composed of items such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items. Depreciation charges for the year totaled \$423,063.

CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2014, the Municipality has \$3,135,485 of cash balance related to proceeds from bond and notes issuances and other restricted assignments that are mainly restricted to future construction activities in the Bond Issue Fund.

Debt Administration

The Puerto Rico Legislative Assembly has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged. The applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes, such Municipality must have sufficient "payment capacity" as defined in Act No. 64. Such Act requires a Municipality must have sufficient "payment capacity" to incur additional general obligation debt if its deposits in the Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, is sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt.

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

The Municipality's financial statements attached hereto, during the earlier months of the present year 2014, the Puerto Rico's Legislative Assembly approved Acts number 18 and 19. Through such legislation, the cash flow produced from collections by the Municipalities of the uses and sales taxes is completely restructured to provide additional liquidity to the Puerto Rico Government Development Bank (GDB) weakened cash position. A new created affiliate to GDB will receive those collections and assumed the total indebtedness incurred by municipalities as of June 30, 2014. A portion of total collections will be used for the payment of debt services requirement. The municipalities included in the new arrangement, advances to the municipalities, free of financing charges, equivalent to the monthly collections from the previous year. In the meantime, total liabilities incurred by the municipalities using Municipal Redemption Fund will be refinanced and GDB will recover its borrowed cash. It is anticipated that under the arrangement, the municipalities will recover the total 1% of uses and sales tax and will get the assurance future sources of financing either from GDB, from new created affiliate or private financing institutions.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available, but the revenue can be also predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2013-2014.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer.

	Governmental Activities	Component Unit Esmeralda del Sur
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,507,091	\$ 160,371
Cash with fiscal agent and restricted deposits	5,358,525	1,324,950
Accounts receivable:		
Property taxes	7,438	
Sales taxes	88,276	
Construction excise taxes	5,959	
Due from commonwealth government	378,099	
Federal government	186,847	
Other receivables	36,066	3,512
Other assets		20,083
Total current assets	<u>7,568,301</u>	<u>1,508,916</u>
Noncurrent assets:		
Land, improvements, and construction in progress	883,445	158,655
Other capital assets, net of depreciation	30,420,217	992,805
Total noncurrent assets	<u>31,303,662</u>	<u>1,151,460</u>
Total assets	<u>\$ 38,871,963</u>	<u>\$ 2,660,376</u>
Liabilities		
Current liabilities:		
Accounts payable and accrued liabilities	1,465,822	23,984
Due to commonwealth government	896,285	
Unearned revenues:		
Municipal license tax	344,215	
Federal grant	54,539	
Bond payable	390,000	
Interest payable	305,882	3,108
Long-Term Liabilities		
Due within one year	1,885,505	170,711
Due in more than one year	18,885,487	457,325
Total liabilities	<u>24,227,735</u>	<u>655,128</u>
Net Position		
Net investment in capital assets	25,413,662	571,924
Restricted for:		
Debt service	1,008,686	
Federal and state funded programs	8,592,741	
Unrestricted (deficit)	<u>(20,370,861)</u>	<u>1,433,324</u>
Total net position	<u>\$ 14,644,228</u>	<u>\$ 2,005,248</u>

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position	
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government	Component Units
					Governmental Activities	Esmeralda del Sur
Primary Government						
General government	\$ 5,554,989	\$ 51,886	\$ -	\$ -	\$ (5,503,103)	\$ -
Public safety	1,050,917				(1,050,917)	
Health and welfare	923,150		146,627	328,006	(448,517)	
Culture and recreation	560,640				(560,640)	
Community development	631,348			598,247	(33,101)	
Public works	3,078,861			1,926,052	(1,152,809)	
Education	1,086,331		1,109,658		23,327	
Interest	672,125				(672,125)	
Total governmental activities	<u>\$ 13,558,361</u>	<u>\$ 51,886</u>	<u>\$ 1,256,285</u>	<u>\$ 2,852,305</u>	<u>\$ (9,397,885)</u>	<u>\$ -</u>
Component units						
Esmeralda del Sur	420,136					(420,136)
Total Component Units	<u>\$ 420,136</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (420,136)</u>
General revenues:						
Property taxes					1,772,165	
Municipal sales and use tax					1,043,458	
Municipal license tax					477,770	
Construction excise tax					196,552	
Rent of property						479,859
Grants and contribution not restricted for specific purpose					7,018,818	
Interest					4,498	6,784
Miscellaneous					339,688	2,601
Total general revenue					<u>10,852,949</u>	<u>489,244</u>
Change in net position					1,455,064	69,108
Net position, beginning of year, as restated					13,189,164	1,936,140
Net position, end of year					<u>\$ 14,644,228</u>	<u>\$ 2,005,248</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PATILLAS**

**BALANCE SHEET - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2014**

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Bond Issue Fund</u>	<u>State Assignments Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets						
Cash and cash equivalents	\$ 131,587	\$ -	\$ -	\$ 808,133	\$ 567,371	\$ 1,507,091
Cash with fiscal agent		2,160,145	3,135,485		62,895	5,358,525
Accounts receivable:						
Property taxes		7,438				7,438
Sales Tax	21,227	67,049				88,276
Construction excise tax	5,959					5,959
Other	36,066					36,066
Due from:						
Commonwealth government	259,281				118,818	378,099
Federal government					186,847	186,847
Due from other funds	765,180			1,969,893	2,435,876	5,170,949
Total assets	<u>\$ 1,219,300</u>	<u>\$ 2,234,632</u>	<u>\$ 3,135,485</u>	<u>\$ 2,778,026</u>	<u>\$ 3,371,807</u>	<u>\$ 12,739,250</u>
Liabilities and Fund Balances						
Liabilities :						
Accounts payable and accrued liabilities	\$ 1,063,225	\$ -	\$ -	\$ 111,889	\$ 290,708	\$ 1,465,822
Due to commonwealth government	895,959				326	896,285
Due to other funds	4,405,770	530,064		10,094	225,021	5,170,949
Unearned revenues:						
Municipal license tax	344,215					344,215
Federal grant revenues					54,539	54,539
Matured bonds due and payable		390,000				390,000
Matured interest due and payable		305,882				305,882
Total liabilities	<u>6,709,169</u>	<u>1,225,946</u>	<u>-</u>	<u>121,983</u>	<u>570,594</u>	<u>8,627,692</u>
Deferred Inflows of Resources						
Unavailable Revenues:						
Commonwealth Government	95,744					95,744
Total Deferred Inflows of Resources	<u>95,744</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>95,744</u>
Fund balances:						
Restricted		1,008,686	3,135,485	2,656,043	2,801,213	9,601,427
Unassigned	(5,585,613)					(5,585,613)
Total fund balances	<u>(5,585,613)</u>	<u>1,008,686</u>	<u>3,135,485</u>	<u>2,656,043</u>	<u>2,801,213</u>	<u>4,015,814</u>
Total liabilities and fund balances	<u>\$ 1,219,300</u>	<u>\$ 2,234,632</u>	<u>\$ 3,135,485</u>	<u>\$ 2,778,026</u>	<u>\$ 3,371,807</u>	<u>\$ 12,739,250</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PATILLAS**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2014**

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Bond Issue Fund</u>	<u>State Assignments Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues						
Property taxes	\$ 1,193,147	\$ 579,018	\$ -	\$ -	\$ -	\$ 1,772,165
Municipal sales and use tax	265,564	777,894				1,043,458
Municipal license taxes	477,770					477,770
Construction excise taxes	196,552					196,552
Intergovernmental grants and contributions	7,021,973			1,920,584	118,818	9,061,375
Interest	4,498				102	4,600
Charge for services	51,886					51,886
Fines and forfeitures	6,080					6,080
Federal grants					2,031,434	2,031,434
Miscellaneous	603,608			1,721	35,931	641,260
Total revenues	<u>\$ 9,821,078</u>	<u>\$ 1,356,912</u>	<u>\$ -</u>	<u>\$ 1,922,305</u>	<u>\$ 2,186,285</u>	<u>\$ 15,286,580</u>
Expenditures						
Current:						
General government	\$ 5,649,433	\$ -	\$ 64,322	\$ -	\$ 8,044	\$ 5,721,799
Public safety	961,404					961,404
Health and welfare	456,183				461,230	917,413
Culture and recreation	547,242					547,242
Community development					612,085	612,085
Public works	2,804,026		133,600	1,126,165	289,269	4,353,060
Education					1,086,331	1,086,331
Debt service:						
Principal		707,000				707,000
Interest		672,125				672,125
Total expenditures	<u>10,418,288</u>	<u>1,379,125</u>	<u>197,922</u>	<u>1,126,165</u>	<u>2,456,959</u>	<u>15,578,459</u>
Excess (deficiency) of revenues over (under) expenditures	(597,210)	(22,213)	(197,922)	796,140	(270,674)	(291,879)
Other financing sources (uses)						
Transfers in	1,077,615	376,735			63,972	1,518,322
Transfers out	(403,325)	(954,149)	(27,400)	(79,134)	(54,314)	(1,518,322)
Total other financing sources (uses)	<u>674,290</u>	<u>(577,414)</u>	<u>(27,400)</u>	<u>(79,134)</u>	<u>9,658</u>	<u>-</u>
Net changes in fund balances	77,080	(599,627)	(225,322)	717,006	(261,016)	(291,879)
Fund balance, beginning as restated	<u>(5,662,693)</u>	<u>1,608,313</u>	<u>3,360,807</u>	<u>1,939,037</u>	<u>3,062,229</u>	<u>4,307,693</u>
Fund balance, ending	<u>\$ (5,585,613)</u>	<u>\$ 1,008,686</u>	<u>\$ 3,135,485</u>	<u>\$ 2,656,043</u>	<u>\$ 2,801,213</u>	<u>\$ 4,015,814</u>

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

Total Fund Balances - Governmental Funds \$ 4,015,814

**Amounts reported for Governmental Activities in the Statement of Net Position
are different because:**

Capital assets used in governmental activities are not financial resources and therefore,
are not reported in the funds. In the current period, these amounts are:

Non depreciable capital Assets	\$ 883,445	
Depreciable capital assets	40,528,482	
Accumulated depreciation	<u>(10,108,265)</u>	
Total capital assets		31,303,662

Other assets are not available to pay current-period expenditures and, therefore,
are reported as deferred inflows of resources in the funds:

Due from Commonwealth Government:		
Christmas bonus reimbursement		95,744

Some liabilities are not due and payable in the current period and therefore, are not
reported in the funds. Those liabilities consist of:

General bonds and notes payable	14,805,000	
Compensated absences	1,211,795	
Claims and judgments	114,760	
Law 42 note payable	1,268,030	
Law 146 note payable	43,511	
Department of Labor-Employment note payable	223,930	
Consolidate Waste debt agreement	1,887,343	
Puerto Rico Aqueduct and Sewer Authority note payable	1,010,487	
Christmas bonus debt	<u>206,136</u>	
Total Long-Term Liabilities		<u>(20,770,992)</u>

Total Net Position of Governmental Activities \$ 14,644,228

Net Change in Fund Balances - Total Governmental Funds \$ (291,879)

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

Governmental funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense:

Expenditures for capital assets	\$ 1,512,255	
Less: Current-year depreciation	<u>(423,063)</u>	1,089,192

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds:

Christmas bonus reimbursement (current year)		95,744
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Revenues reported in the funds that are not reported as revenues in the Statement of Activities:

Christmas bonus reimbursement (prior year)	(98,899)	
Claims and judgements (prior year)	<u>(270,000)</u>	(368,899)

Repayment of long-term debt is an expenditure in the governmental funds, but reduces long-term liabilities in the Statement of Net Position. In the current year the repayments were:

707,000

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures:

Decrease in compensated absences debt	23,142	
Decrease in Law 42 note payable	35,912	
Decrease in Law 146 note payable	2,417	
Decrease in Puerto Rico Aqueduct and Sewer Authority debt	143,763	
Increase in note payable - Department of Labor	(74,792)	
Decrease in consolidate Waste Debt	93,259	
Increase in claims and Judgments	(6,589)	
Decrease in christmas Bonus	<u>6,794</u>	<u>223,906</u>

Change in Net Position of Governmental Activities

\$ 1,455,064

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Patillas** (the Municipality) was founded in the year 1811. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a fourteen member Municipal Legislature who are elected for a four-year term.

The Municipality provides public safety, public works, culture and recreation, health and welfare, urban development, education, economic development, and other miscellaneous services.

The basic financial statements of the Municipality have been prepared in conformity with Generally Accepted Accounting Principles as applied to local governmental units in the United States of America (US GAAP).

The Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. The Statement was adopted for the fiscal year ended June 30, 2004. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

The Municipality adopted the provisions of GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* (GASB No. 55), and GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards* (GASB No. 56).

GASB No. 55 incorporated the hierarchy of USGAAP for state and local governments into the Governmental Accounting Standards Board's (GASB) authoritative literature. The requirements in this Statement codify all USGAAP for state and local governments so that they derive from a single source.

GASB No. 56 incorporated into the Governmental Accounting Standards Board's (GASB) authoritative literature certain accounting and financial reporting guidance presented in the American Institute of Certified Public Accountants' Statements on Auditing Standards. This Statement addressed three issues not included in the authoritative literature that establishes *accounting* principles-related party transactions, going concern considerations, and subsequent events.

In fiscal year 2012, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which modified the interpretations of certain terms within the definition of the special revenue funds and the types of activities the Municipality may choose to report in those funds. GASB No. 54 also clarified the capital projects fund type definition for better alignment with the needs of preparers and users. Definitions of other governmental fund types were also modified for clarity and consistency.

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

The GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements* (GASB 62), incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance included in FASB pronouncements, which does not conflict with or contradict GASB pronouncements, and eliminates the criteria to apply post-November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements.

In prior year, the Municipality adopted the provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* establishing a new statement of net position format that reports separately all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). The Statement requires deferred outflows of resources and deferred inflows of resources to be reported separately from assets and liabilities. The financial reporting impact resulting from the implementation of GASB 63 in the Municipality's financial statements was the renaming of "Net Assets" to "Net Position", including changing the name of the financial statement from "Statement of Net Assets" to "Statement of Net Position".

A. Component Units

In evaluating how to define the Municipality for financial reporting purposes, Management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, an amendment of Statements No. 14 and 34. This Statement modifies certain requirements for inclusion of components units in the financial reporting entity and amends the criteria for reporting component units as if they were part of the primary government under certain circumstances. The basic, but not the only criterion for including a potential component unit within the reporting entity is if a primary government is financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. Based on the above criteria, the Municipality has one component unit to include within its reporting entity, "Esmeralda del Sur" which is reported as a discretely presented component unit.

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

A. Component Units (Continued)

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 low and/or moderate income individuals in the Patillas 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 Legislature. The mayor of the Municipality is a permanent member of the board of directors.

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. This subsidy is considered a major program. 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 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 regulatory agreement, the Project is required to set aside specified amounts for the replacement of property and other project expenditures approved by HUD. HUD restricted deposits, which approximate \$1,324,950 at June 30, 2014 and \$1,306,538 at June 30, 2013, are held in separate accounts and generally are not available for operating purposes.

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

A. Component Units (Continued)

The project maintains a restricted cash account for insurance escrow. In addition, 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 account. Restricted funds are held in separate accounts and are not available for operating purposes.

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.

As of June 30, 2014 and 2013, 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 statement of net position. The estimated liability of \$48,500 was obtained from the project's comprehensive ACM survey. It is reasonably possible that the estimate of the obligation may change in the near term.

Mortgage Payable

Consist of 9% (with effective subsidy rate of 8%) mortgage note used for construction of the project's buildings, payable in monthly installments of \$16,757, including interest, until 2018, collateralized with land and building.

Debt service requirements in future years are as follows:

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2015	\$ 170,711	\$ 30,368
2016	186,725	14,354
2017	204,241	970
2018	<u>17,859</u>	<u>-</u>
	<u>\$ 579,536</u>	<u>\$ 45,692</u>

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

B. Government-wide and fund financial statements

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

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

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

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. Pursuant to the provisions set forth by GASB No. 54, the Municipality reported the following governmental funds in the accompanying GFFS:

General Fund – is the Municipality main operating fund used to account for and report all financial and reported resources and governmental activities, except for those required to be accounted for in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) USGAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund. Its revenues consist mainly of taxes, licenses and permits, intergovernmental, charges for services and other.

Bond Issues Fund – is a major governmental used to account for and report the proceeds of bonds and notes that are legally restricted or committed to expenditure for specified purposes and for capital projects.

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

B. Government-wide and fund financial statements (Continued)

State Assignment Fund – This is the fund used to account for all the transactions of the State Assignment by Legislature Resolutions. The primary objectives of this assignment are the development of projects on communities, not-for-profit organizations and indirect assignment to persons of low and moderate income.

Debt Service Fund – is a major governmental fund used to account for and report for the accumulation of financial resources that are restricted for, and the payment of, principal and interest for: (1) bonds payable for which debt service payments are legally mandated to be accounted for in a debt service fund and (2) certain special long-term obligations for which the Municipality is accumulating financial resources in advance to pay principal and interest payments maturing in future years.

The outstanding balance of certain general long-term obligations for which debt service payments do not involve the advance accumulation of resources (such as certain notes payable, obligations under capital leases, accrued compensated absences, landfill obligation, claims and judgments, net pension liability and other long-term obligations) are only accounted for in the accompanying statement of net position. The debt service payments of such obligations are generally accounted for in the governmental fund which accounted for the financial resources used for the payment of such debts. Principal and interest due on July 1 of the following fiscal year are accounted for as a fund liability, if resources are available as of June 30 for its payment.

The other governmental funds of the Municipality account for grants and other resources whose use is restricted to a particular purpose.

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

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

C. Financial reporting presentation

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

Government has established the following fund categories, fund types, account group and discrete presentation of enterprise fund:

Governmental Fund Types

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

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

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

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

D. Measurement focus, basis of accounting and financial presentation

Government-wide financial statements – The accompanying GWFS are prepared using the economic resources measurement focus and the accrual basis of accounting. Subject to the additional rules and limitations detailed below, revenues (including interest on deposits and investments) are generally recorded when earned and expenses are generally recorded when a liability is incurred, regardless of the timing of related cash flows.

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange-like transactions are generally recorded when exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values. An exchange-like transaction is one when there is an identifiable exchange and the values exchanged, though related, may not be quite equal. The accompanying basic financial statements include exchange-like transactions such as license fees, fines, penalties, forfeitures, permits, charges for services, and most miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received.

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

D. Measurement focus, basis of accounting and financial presentation (continued)

The Municipality groups its non-exchange transactions into the following four (4) classes in the accompanying basic financial statements: (a) derived tax revenues, (b) imposed non-exchange revenues, (c) government mandated non-exchange transactions, and (d) voluntary non-exchange transactions.

In the case of derived tax revenue transactions, which result from assessments that the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred such as municipal license tax and sales and use tax.

In the case of imposed non-exchange revenue transactions (such as property taxes), which result from assessments made by the Municipality on non-governmental entities, including individuals, other than assessments on exchange transaction, receivables are generally recorded in the period when an enforceable legal claim has arisen. Property taxes and municipal license taxes are generally recorded as revenues (net of amounts considered not collectible) in the fiscal year when resources are required to be used for the first fiscal year that the use of the resources is permitted.

For government-mandated non-exchange transactions (such as intergovernmental grants and contributions), receivables and revenues are generally recorded when all eligibility requirements imposed by the provider have been met. For the majority of grants, the Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Therefore, revenue is generally recognized as qualifying reimbursable expenditures are incurred.

For voluntary non-exchange transactions (such as donations and certain grants and entitlements) receivables and revenues are generally accounted for in the same manner as government-mandated non-exchange transactions discussed above.

Interests on deposits are recorded when earned since these revenues are considered both measurable and available at June 30, 2014. Receipts of any type of revenue sources collected in advance for use in the following fiscal year are recorded as unearned revenues.

According to GASB No. 34, all general capital assets and the unmatured long-term liabilities are recorded only in the accompanying Statement of Net Position. The measurement focus and the basis of accounting used in the accompanying GWFS differ significantly from the measurement focus used in the preparation of the GFFS. Therefore, the accompanying GFFS include reconciliations, as detailed in the accompanying table of contents, to better identify the relationship between the GWFS and the GFFS.

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

D. Measurement focus, basis of accounting and financial presentation (continued)

Government Fund Financial Statements – The accompanying GFFS are reported using the current financial resources measurements focus and the modified-accrual basis of accounting. Revenues are generally recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current fiscal year or soon enough thereafter to pay liabilities of the current fiscal year. For this purpose, the Municipality generally considers most revenues (municipal licenses taxes, construction excise taxes, sales and use taxes, interests on deposits, intergovernmental grants and contributions and certain charges for services) to be available if collected within sixty (60) days after June 30, 2014. At June 30, 2014, all revenues sources met this availability criterion.

Property taxes are all considered susceptible to accrual if commonly collected within sixty (60) days following the end of the fiscal period, unless unusual circumstances justify a greater period.

Other revenue sources considered susceptible to accrual include municipal license taxes, sales and use taxes, construction excise taxes, intergovernmental grants and contributions, interests on deposits and charges for services. These principal revenue sources meet both measurability and availability criteria in the accompanying GFFS.

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed above, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange, exchange-like transactions are also generally recorded when the exchange takes place while all revenues, expenses, gains, losses, and assets resulting from non-exchange transactions are recorded when an enforceable legal claim arises or when all eligibility requirements imposed by the provider have been met, applicable.

Pursuant to the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements* (GASBI No. 6), in the absence of an explicit requirement (i.e., the absence of an applicable modification, discussed below) the Municipality generally accrues a governmental fund liability and expenditure (including salaries, professional services, supplies, utilities, etc.) in the period in which the government incurs the liability, to the extent that these liabilities are normally expected to be liquidated in a timely manner and in full with current available financial resources. The accompanying Balance Sheet – Governmental Funds generally reflects only assets that will be converted into cash to satisfy current liabilities. Long-term assets and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying Balance Sheet – Governmental Funds. At the same time, long-term liabilities (generally, those unmatured that will not require the use of current financial resources to pay them) are not accounted for in the accompanying Balance Sheet – Governmental Funds.

The measurement focus of the GFFS is on decreases of net financial resources (expenditures) rather than expenses. Most expenditures are measurable and are recorded when the related governmental fund liability is incurred. Allocation of costs, such as depreciation and amortization, are recorded in the accompanying Statement of Activities, but are not recorded in the accompanying GFFS.

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

E. Assets, liabilities and net position

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

Cash with fiscal agent in the debt service fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law. Also, cash with fiscal agent consists of unused proceeds of bonds and notes issued for the acquisition of equipment and construction of major capital improvements.

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

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

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables in the General Fund represent mostly contributions from the Puerto Rico Electric Power Authority, which contribute a specific percentage of their revenues as payment in lieu of taxes. Intergovernmental receivable in the special revenue fund represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs.

3. **Inventories** - Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net position.
4. **Capital assets** - Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. Capital assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

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

E. Assets, liabilities and net position (Continued)

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

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

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Vehicles, Heavy Equipment	5 to 25 years	\$300
Furniture and Fixture	5 to 10 years	\$300
Computer and Electronic Equipment	5 years	\$300
Buildings	50 years	\$1
Infrastructure	60 years	\$1
Improvements	20 to 40 years	\$1

5. Unearned revenues - Unearned revenues arises when one of the following situations occur:

- a. Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period (unavailable revenue). As previously discussed, available is defined as due (or past due) at June 30, 2014 and collected within 60 days thereafter to pay obligations due at June 30. In subsequent periods, when both criteria are met, the liability for unearned revenue is removed and revenue is recognized.
- b. The Municipality receives resources before it has a legal claim to them (unearned revenue). In subsequent periods, when the revenue recognition criterion is met, the liability for unearned revenue is removed and revenue is recognized.

Unearned revenues at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them.

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

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

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

E. Assets, liabilities and net position (continued)

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

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality. All sick leave pay and salary related benefits are accrued when incurred in the governmental-wide financial statements when the employee meets such criteria.

8. **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 when the liability is incurred.

9. **Fund Balances** - In fiscal year 2012, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which enhanced the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied. This statement establishes fund balance classifications that comprise a hierarchy upon the use of the resources reported in governmental funds.

Pursuant to the provisions of GASB No. 54, the accompanying GFFS report fund balance amounts that are considered restricted, committed, assigned, and unassigned, based on the relative strength of the constraints that control how specific amounts can be spent, as described as follows:

- a. **Restricted** - Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditors or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- b. **Committed** - Represent resources used for specific purposes, imposed by formal action of the Municipal's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.

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

E. Assets, liabilities and net position (continued)

- c. **Assigned** – Represent resources intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed (generally executive orders approved by the Mayor). Intent can be expressed by the Municipal Legislature, the Mayor or by an official or body to which the Municipal legislature delegates authority in conformity with the Autonomous Municipalities Act of Puerto Rico, as amended. In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.
- d. **Unassigned** - Represent the residual classification for the Municipality's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

Negative fund balance amounts are assigned amounts reduced to the amount that will raise the fund balance to zero. Consequently, negative residual amounts in restricted, committed and assigned fund balance classifications have been reclassified to unassigned fund balances.

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balances amounts as of for the fiscal year ended June 30, 2014.

In situations when expenditure is made for a purpose for which amounts are available in multiple fund balance classifications, the Municipality generally spends restricted resources first, and then unrestricted resources. Within unrestricted resources, the Municipality generally spends committed resources first, followed by assigned resources, and then unassigned resources.

- 10. **Net Position** - has been reported pursuant to the provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. Net Position represents the difference between all assets plus deferred outflows of resources and all liabilities plus deferred inflows of resources. The Net Position consists of net resources restricted by external parties (such as debt covenants, creditors, grantors, contributions, laws or regulations of other governments, etc.), or net position for which constraints are imposed by the constitutional provisions or enabling legislation.

Enabling legislation consists of legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

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

E. Assets, liabilities and net position (continued)

A legally enforceable enabling legislation restriction is one that a party external to the Municipality (such as citizens, public interest groups, or the judiciary) can compel the Municipality to honor. The Municipality periodically reevaluates the legal enforceability of an enabling legislation to determine if any of the resources raised by the enabling legislation are used for a purpose not specified by the enabling legislation or if the Municipality has other cause for consideration.

The classification of restricted net position identifies resources that have been received or earned by the Municipality with an explicit understanding between the Municipality and the resource providers that the resources would be used for specific purposes. Grants, contributions and donations are often given under those kinds of conditions. Bond indentures also often limit the use of bond proceeds to specific purposes.

Internally imposed designation of resources, including earmarking, are not reported as restricted net position. These designations consist of management's plans for the use of resources, which are subject to change at the discretion of the Municipal Legislature.

In the government-wide statements, net position is segregated into three categories:

- a. **Net Investment in capital assets:** Represent the component of the net position that consist of capital asset balances net of accumulated depreciation and amortization reduced by the outstanding balances of any bonds, notes and other borrowings that are attributable to the acquisition, construction, or improvement of those assets. This category should not include cash that is restricted to capital assets acquisition or construction (unspent bond proceeds).
- b. **Restricted net position:** Represents the component of the net position that is subject to restrictions beyond the Municipal's control. These include restrictions that are externally imposed (by creditors, grantors, contributors, or laws and regulations of other governments) or restrictions imposed by the law through constitutional provisions or enabling legislation (including enabling legislation passed by the government itself).
- c. **Unrestricted net position:** Represents the component of the net position that do not meet the definition of net position invested in capital assets or restricted. Unrestricted assets are often designated to indicate that Management does not consider them to be available for general operations. These types of constraints are internal and Management can remove or modify them. Designations are not reported on the face of the Statement of Net Position.

11. **Accounting for Pension Costs** - the provisions of GASBS No. 50, *Pension Disclosure*, which amended GASBS No. 27, *Accounting for Pensions by State and Local Government Employers*, by requiring disclosure of how the contractually required contribution rate is determined by governments participating in multi-employer cost-sharing pension plans.

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

E. Assets, liabilities and net position (continued)

The Municipality accounts for pension costs from the standpoint of a participant in a multi-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

For the purpose of applying the requirements of GASBS No. 27, the state government of the Government of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) and System 2000, a multi-employer cost-sharing defined benefit pension plan and a hybrid defined contribution plan, respectively, in which the employees of the Municipality participate. The Municipality is considered a participant, and not a sponsor, of these retirement systems since the majority of the participants in the aforementioned pension trust funds are employees of the Government of Puerto Rico and the basic financial statements of such retirement systems are part of the financial reporting entity of the Government of Puerto Rico.

12. Interfund and intra-entity transactions - The Municipality has the following types of transactions among funds:

- a. Operating Transfers** - Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
- b. Intra-Entity Transactions** - Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.

13. Risk financing - The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the CRIM for the year ended June 30, 2014 to \$181,120. The current insurance policies have not been cancelled or terminated.

The Municipality carries insurance coverage for death and bodily injuries caused by the automobile accidents.

The insurance is obtained through the Automobile Accidents Compensation Administration (AACA), a component unit of the Commonwealth of Puerto Rico. This insurance is compulsory for all licensed vehicles used on public roads and highways in Puerto Rico. The annual premium is \$35 per licensed motor vehicle, which is paid directly to AACA.

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

E. Assets, liabilities and net position (continued)

The Municipality obtains workers' compensation insurance through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth of Puerto Rico. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center (CRIM) for the year ended June 30, 2014 amounted to \$169,510.

The Municipality obtains unemployment compensation, non-occupational disability, and drivers' insurance coverage for its employees through various insurance programs administered by the Commonwealth of Puerto Rico's Department of Labor and Human Resources (DOL). These insurance programs cover workers against unemployment and provide supplementary insurance coverage for temporary disability, or death because work or employment-related accidents or non-occupational disability and drivers' insurance premiums are paid directly to DOL on a cost reimbursement basis.

- 14. Use of Estimates** - The preparation of financial statements in conformity with USGAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual amounts could differ from those estimates.

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2. CASH AND CASH EQUIVALENTS

The Municipality maintains its deposits in various commercial banks located in Puerto Rico and Government Development Bank for Puerto Rico (GDB). Proceeds from bonds and funds related to certain grant awards are required by law to be held with GDB.

The Municipality adopted the provisions of GASB Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate risk, (3) custodial credit risk, (4) foreign exchange exposure.

Credit risk - This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial and credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly the Municipality invests only in obligations of the Commonwealth, obligations of the United States of America, certificates of deposits, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality does not invest in marketable securities or any types of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2014.

Interest rate risk - This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investment portfolio at June 30, 2014, (2) limiting the weighted average maturity of its investments to three months or less, and (3) keeping most of its bank deposits in interests bearing accounts generating interests at prevailing market rates. At June 30, 2014, the Municipality's investments in certificates of deposits are recorded at cost, which approximates their fair value. Therefore, the Municipality's management has concluded that at June 30, 2014, the interest rate risk associated with the Municipality's cash and cash equivalents is considered low.

Custodial credit risk - In the case of deposits, this is the risk that in the event of a bank failure, the Municipality's deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico* the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC) generally up to a maximum of \$250,000 per depositor.

In addition, public funds deposited in commercial banks by the Municipality are fully securities pledged as collateral are held, in the Municipality's name, by the agents of the Commonwealth's Secretary of Treasury. Deposits with GDB are uninsured and uncollateralized.

However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2014. Therefore, the Municipality's management has concluded that at June 30, 2014, the custodial credit risk associated with the Municipality's cash and cash equivalents is considered low.

2. CASH AND CASH EQUIVALENTS (CONTINUED)

Foreign exchange risk - The risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, the Municipality is prevented from investing in foreign securities or any other types of investments in which foreign exchange risk exposure may be significant. Accordingly, Management has concluded that the foreign exchange risk related to the Municipality's deposits is considered low at June 30, 2014. Under Commonwealth of Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

Deposits - The Municipality's bank balances in commercial banks of \$131,587 in the general fund, \$808,133 in the state assignments fund and \$567,371 in the others governmental funds were fully collateralized at June 30, 2014.

The deposits at GDB of \$2,160,145 in the debt service fund and \$3,135,485 in the bond issue fund that is restricted are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

A. *Municipal License Tax* - The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$3,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2014, the tax rates were as follows:

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

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year is recorded as unearned revenues.

B. *Due from Commonwealth Government* - In the general fund, the amount of \$259,281 represents \$163,537 of due from the Municipal Revenue Collection Center related to retentions made in excess for the payment of a debt with the Retirement System Administration and \$95,744 related to Christmas bonus state compensation.

C. *Due from Commonwealth government* - the receivable of \$118,818 from Commonwealth government in the other governmental funds represent expenditures incurred not yet reimbursed by the Department of Labor, related to the Law 52 proposal.

3. RECEIVABLES (CONTINUED)

D. Due from Federal Government – the receivable from Federal government in the other governmental funds represent mainly expenditures incurred not yet reimbursed by the Federal Government. Following is a detail of the federal grant receivables:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grants- State's Program	\$ 140,719
Community Service Block Grant	190
Child Care and Development Block Grant	434
Head Start Program	45,504
Total	<u>\$ 186,847</u>

4. INTERFUND TRANSACTIONS

During the course of operations, numerous transactions occur between individual funds that may result in amounts owed between funds. Those related to goods and services type transactions are classified as “due to and from other funds” (i.e., current portion of interfund loans).

Interfund receivables and payables at June 30, 2014 are summarized as follows:

a. Due from/to other fund:

<u>Fund</u>	<u>Receivable Fund</u>	<u>Payable Fund</u>
General Fund	\$ 765,180	\$ 4,405,770
Debt Service Fund		530,064
State Assignments Fund	1,969,893	10,094
Other Governmental Funds	2,435,876	225,021
Total	<u>\$ 5,170,949</u>	<u>\$ 5,170,949</u>

b. Transfer in/out to other fund

Following is a summary of interfund transfers for the year:

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Debt Service Fund	Transfers funds to cover debt service payments	\$ 376,735
General Fund	Other Governmental Funds	Transfers funds to cover special funds expenditures	26,590
Debt Service Fund	General Fund	Transfers of excess in debt service cash balance	954,149
Bond Issue Fund	General Fund	Transfers funds to cover operational expenditures	27,400
State Assignments Fund	General Fund	Transfers funds to cover operational expenditures	79,134
Other Governmental Funds	General Fund	Transfers funds to cover operational expenditures	16,932
Other Governmental Funds	Other Governmental Funds	Transfers funds to cover special funds expenditures	37,382
Total Governmental Fund Financial Statements			<u>\$ 1,518,322</u>

5. CAPITAL ASSETS

Capital assets; those with an estimated useful live of one year or more from the time of acquisition by the Municipality and a cost of \$300 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2014, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<u>Governmental Activities:</u>	<u>Balance July 1, 2013</u>	<u>Additions</u>	<u>Retirements/ Reclassifications</u>	<u>Balance June 30, 2014</u>
Capital asset, not being depreciated:				
Construction in progress	\$ 268,165	\$ 423,081	\$ -	\$ 691,246
Land	<u>192,199</u>	<u>-</u>	<u>-</u>	<u>192,199</u>
Total capital assets not being depreciated	<u>460,364</u>	<u>423,081</u>	<u>-</u>	<u>883,445</u>
Capital assets, being depreciated:				
Buildings and building improvements	14,108,574	105,052		14,213,626
Infrastructure	20,120,808	755,727		20,876,535
Equipments	2,252,620	77,500		2,330,120
Vehicles	<u>2,957,306</u>	<u>150,895</u>	<u>-</u>	<u>3,108,201</u>
Total capital assets being depreciated	<u>39,439,308</u>	<u>1,089,174</u>	<u>-</u>	<u>40,528,482</u>
Less accumulated depreciation for:				
Buildings and building improvements	(4,651,208)	(184,451)		(4,835,659)
Infrastructure	(249,836)	(70,329)		(320,165)
Equipments	(1,952,074)	(135,542)		(2,087,616)
Vehicles	<u>(2,832,084)</u>	<u>(32,741)</u>	<u>-</u>	<u>(2,864,825)</u>
Total accumulated depreciation	<u>(9,685,202)</u>	<u>(423,063)</u>	<u>-</u>	<u>(10,108,265)</u>
Total capital assets being depreciated, net	<u>29,754,106</u>	<u>666,111</u>	<u>-</u>	<u>30,420,217</u>
Governmental activities capital assets, net	<u>\$ 30,214,470</u>	<u>\$ 1,089,192</u>	<u>\$ -</u>	<u>\$ 31,303,662</u>

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

<u>Governmental activities:</u>	<u>Amount</u>
General government	\$ 6,330
Public safety	89,513
Public works	288,822
Health and welfare	5,737
Culture and recreation	13,398
Community development	<u>19,263</u>
Total depreciation expense-governmental activities	<u>\$ 423,063</u>

6. PROPERTY TAXES

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

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections, as modified by the quarterly revisions of estimates required law. The CRIM is required by law to prepare a liquidation statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This preliminary liquidation has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final liquidation made not later than six months after year-end, subject to the verification by its Independent Auditors. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30.

On January 26, 2000, Public Law No. 42 was enacted, which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000. The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238, enacted on August 15, 1999. On October 11, 2001, Public Law No. 146 was enacted to amend Public Law No. 42, to extend the loan amortization period up to 30 years. Also, on October 11, 2002, Public Law No. 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law No. 42 enacted on January 26, 2000. The Statement of Net Position includes an outstanding debt balance of \$1,268,030 at June 30, 2014, related with Law No. 42.

On June 26 1997, Public Law No. 21 was enacted, which authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owed property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable o equivalent in money.

6. PROPERTY TAXES (CONTINUED)

Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law No. 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities through a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law. The Statement of Net Position includes an outstanding debt balance of \$43,511.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the Puerto Rico Treasury Department assumes payment of the basic tax to the Municipalities, except for property assessed at less than \$3,500 for which no payment is made. As part of the Municipal Autonomous Law of 1991, the exempt amount to be paid by the Puerto Rico Treasury department to the Municipalities was frozen as of January 1, 1992. In addition, the law grants a tax exemption from the payment of personal property taxes of up to \$50,000 of the assessed value to retailers having annual net sales of less than \$150,000.

The annual tax rate is 10.33% for real property and 8.33% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the General Fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.75% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund. The Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected and such amount is accounted for similar to item (a) above.

7. MUNICIPAL SALES AND USE TAX

On July 29, 2007, an amendment to Act No. 117 of July 4, 2006, known as the "Tax Fairness Act of 2006", was enacted with the purpose of establishing a mandatory sales and use tax of 1.5% at the Municipal Level. 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 the Treasury Department. The Act provides an optional surtax on the un-process food. This surtax must be approved by the Municipal Legislature. The Treasury Department is responsible to create, the Municipal Development Fund (.2%), the Municipal Redemption Fund (.2%) and the Municipal Improvements Fund (.1%) with the remaining 0.5%. The Municipality collected \$ 1,043,458 during the year ended June 30, 2014.

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2014 are summarized as follows:

<u>Description</u>	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Bond Issue Fund</u>	<u>State Assignments Fund</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Accounts payable	\$ 984,518	\$ -	-	\$ 111,889	\$ 290,708	\$ 1,387,115
Accrued liabilities	<u>78,707</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>78,707</u>
Total	<u>\$ 1,063,225</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 111,889</u>	<u>\$ 290,708</u>	<u>\$ 1,465,822</u>

9. DUE TO COMMONWEALTH GOVERNMENT

The amounts due to Commonwealth Government in the general fund and other governmental funds include the following:

<u>Governmental Entity</u>	<u>Amount</u>
Commonwealth of Puerto Rico Employees Association (AEGPR)	\$ 54,928
Retirement System Administration	341,103
Puerto Rico Aqueduct and Sewer Authority	98,677
Internal Revenue Service	28,976
General Services Administration	243,331
Puerto Rico Treasury Department	13,381
Claro Puerto Rico	9,476
Municipal Revenue Collection Center	100,522
Department of Labor	5,565
Others	<u>326</u>
Total	<u>\$ 896,285</u>

10. UNEARNED REVENUES

A. Municipal License Tax- The unearned revenues of \$344,215 in the general fund relates to municipal license tax collected in fiscal year 2013-14 that will be earned in fiscal year 2014-15.

11. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2014, was as follows:

Description	Beginning Balance, as restated	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds payable	\$ 10,562,000	\$ -	\$ (352,000)	\$ 10,210,000	\$ 371,000
Notes payable	5,320,000		(335,000)	4,985,000	360,000
Public Act No. 42 January 20, 2001 note payable	1,303,942		(35,912)	1,268,030	38,168
Public Act No. 146 of October 11, 2001 note payable	45,928		(2,417)	43,511	2,417
Compensated Absences PR Department of Labor – Payment plan	1,234,937		(23,142)	1,211,795	200,000
Claims and judgments	149,138	117,764	(42,972)	223,930	74,640
Puerto Rico Aqueduct and Sewer Authority - Debt agreement	108,171	6,589		114,760	
Consolidate Waste Debt agreement	1,154,250	95,048	(238,811)	1,010,487	333,144
Christmas bonus	1,980,602	86,741	(180,000)	1,887,343	300,000
	<u>212,930</u>	<u>206,136</u>	<u>(212,930)</u>	<u>206,136</u>	<u>206,136</u>
Total	<u>\$ 22,071,898</u>	<u>\$ 512,278</u>	<u>\$ (1,423,184)</u>	<u>\$ 21,160,992</u>	<u>\$ 1,885,505</u>

- 1. Legal Debt Margin** - The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds payable, is paid with unrestricted funds.
- 2. Bonds Payable** - The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. Bonds payable outstanding at June 30, 2014 are as follows:

Description	Balance at June 30, 2014
1997 Special obligation bond for the construction of capital assets with an original amount of \$400,000 due in annual installments of \$10,000 to \$40,000, through July 1, 2016, with interest of 1.53% to 8.00%	\$ 70,000
2002 General obligation bond for construction and reconstruction of Municipality's infrastructure with an original amount of \$2,740,000 due in annual installments of \$45,000 to \$215,000 through July 1, 2026, with interest of 2.70% to 5.60%	1,935,000
2002 General obligation bond for the acquisition of real estate with an original amount of \$255,000 due in installments of \$5,000 to \$20,000 through July 1, 2026, with interest ranging from 2.70% to 5.60%	180,000

11. LONG-TERM LIABILITIES (CONTINUED)

Description	Balance at June 30, 2014
2007 General obligation bond for the reconstruction of infrastructure with an original amount of \$100,000 due in installments of \$5,000 to \$10,000 through July 1, 2021, with interest ranging from 1.53% to 7.50%	65,000
2007 General obligation bond for construction of infrastructure with an original amount of \$410,000 due in installments of \$5,000 to \$40,000 through July 1, 2031, with interest ranging from 1.53% to 7.50%	360,000
2008 Special obligation bond to compensate general obligations with an original amount of \$464,000 due in installments of \$33,000 to \$62,000 through July 1, 2018, with interest ranging from 1.53% to 7.50%	225,000
2008 General obligation bond to compensate the General Fund and for improvement of infrastructure with an original amount of \$375,000 due in installments of \$5,000 to \$30,000 through July 1, 2033, with interest ranging from 1.53% to 7.50%	350,000
2011 Special obligation bond with an original amount of \$3,460,000 due in installments of \$55,000 to \$280,000 through July 1, 2035, with interest ranging from 6.00% to 7.00%	3,280,000
2011 Special obligation bond for debt payment with an original amount of \$750,000 due in installments of \$30,000 to \$80,000 through July 1, 2025, with interest ranging from 6.00% to 7.00%	690,000
2012 General obligation bond for the payment of several statutory debts with an original amount of \$3,160,000 due in installments of \$50,000 to \$205,000 through July 1, 2033, with interest ranging from 6.00% to 7.00%	<u>3,055,000</u>
Total	<u>\$ 10,210,000</u>

These bonds, except the 2008 Series \$464,000 and the 1997 Series \$400,000 bonds, are payable from the special ad valorem property tax of 4% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes. The before detailed bonds are payable with General Fund resources. The 2011 Series \$3,460,000 and the 2011 Series \$750,000 bonds are payable with the revenues generated from the collection of the .2% of the municipal sales and use tax imposed by the Municipality and collected by the Puerto Rico Treasury Department.

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

Year Ending June 30,	Principal	Interest
2015	\$ 371,000	\$ 640,180
2016	399,000	619,843
2017	383,000	609,187
2018	412,000	599,197
2019	380,000	571,267
2020-2024	2,315,000	2,441,843
2025-2029	2,490,000	1,599,728
2030-2034	2,210,000	839,875
2035-2039	1,250,000	115,500
Total	<u>\$ 10,210,000</u>	<u>\$ 8,036,620</u>

11. LONG-TERM LIABILITIES (CONTINUED)

3. **Notes Payable** - The proceeds of the issuance of notes payable were used principally to pay debt incurred in prior years and to cover the expenditures of a special event. The notes are payable as follows:

Type of notes	Maturity Date	Original Amount	Range of Interest rates	Balance at June 30, 2014
2008 Special obligations notes	7-1-32	4,850,000	1.53% to 7.00%	\$ 4,440,000
2009 Special obligations notes	7-1-16	895,000	4.75% to 7.50%	305,000
2009 Special obligations notes	7-1-16	705,000	4.75% to 7.50%	240,000
Total notes payable				<u>\$ 4,985,000</u>

The 2008 Series \$4,850,000 note is payable with the revenues generated from the collection of the .2% of the municipal sales and use tax imposed by the Municipality and collected by the Puerto Rico Treasury Department. The 2009 Series \$895,000 and 2009 Series \$705,000 notes are payable with General Fund resources. Annual debt service requirements to maturity for notes payable are as follows:

Year Ending June 30, 2014	Principal	Interest
2015	\$ 360,000	\$ 304,275
2016	385,000	278,775
2017	110,000	251,100
2018	120,000	244,200
2019	125,000	236,850
2020-2024	990,000	1,037,400
2025-2029	1,420,000	708,725
2030-2034	1,475,000	215,775
Total	<u>\$ 4,985,000</u>	<u>\$ 3,277,100</u>

4. **Property Taxes Debts (Law No. 146 and Law No. 42)** – These amounts represents the balance owed to the Municipal Revenue Collection Center (“CRIM”) at June 30, 2014 as explained in Note 6.
5. **Compensated Absences** – The government-wide statement of net position includes \$1,211,795 of accrued sick leave and vacation benefits, representing the Municipality’s commitment to fund such costs from future operations.
6. **Department of Labor Repayment Plan** – This amount represent the balance owed to the Department of Labor related with unemployment compensation.
7. **Claims and Judgments** – The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund when the liability is incurred.
8. **Puerto Rico Aqueduct and Sewer Authority - Debt Agreement** – This amount represent the balance owed to the Puerto Rico Aqueduct and Sewer Authority related to water and sewer utility changes.
9. **Consolidate Waste Debt Agreement** – This amount represent the balance owed to the company contracted for waste disposal.
10. **Christmas bonus** - This amount represents the accrued portion corresponding to the fiscal year 2014 of the Christmas bonus to be paid in December 2014.

12. PENSION PLAN

A. Act No. 447 and System 2000 (until June 30, 2013)

As of June 30, 2014 regular employees of the Municipality contribute to a cost-sharing multiple employer defined benefit retirement plan administered by the Employee's 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, the municipalities of Puerto Rico and certain public corporations not having their own retirement systems. The system provides retirement pensions, death, and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

The system operates under *Act 447, approved on May 15, 1951* effective on January 1, 1952 and *Act 1 of February 16, 1990* for employees that entered as participants of the Plan starting April 1, 1990 and ending December 31, 1999. Under this Act, retirement benefits were determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation was computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member was eligible, was limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS.

Act No. 305 of September 24, 1999 amended *Act. No. 447 of 1951* and *Act 1 of February 16, 1990* to establish a new pension program (System 2000). The new pension program became effective on January 1, 2000. Employees participating in the Act 447 system as of December 31, 1999 had the choice to either stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000 were only allowed to become members of the new program. System 2000 was a hybrid defined contribution plan, also known as a cash balance plan.

There would be a pool of pension assets, which would be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age would not be guaranteed by the State government and would be subjected to the total accumulated balance of the savings account. The annuity would be based on a formula, which assumed that each year the employee's contribution (with a minimum of 8.275% of the employee's salary up to a maximum of 10%) would be invested in an account which would either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. If the savings accounts balance was \$10,000 or less at time of retirement, the balance would be distributed by the System to the participant as a lump sum. Participants received periodic account statements similar to those of defined contribution plans showing their accrued balances. The employer contributions (11.275% of the employee's salary) would be used to fund the plan. Under System 2000 the retirement age was reduced from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

The Act No. 447, as amended, was the authority under which obligations to contribute to the Plan by the Plan members, employers and other contributing entities were established or amended. Plan members were required to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600 except for the Mayor or employee under a supplementation plan, which contributed 8.275%

12. PENSION PLAN (CONTINUED)

of gross salary. In order to address the unfunded actuarial accrued liability of the System, on July 6, 2011 (effective July 1, 2011) the Commonwealth Legislature approved Act No. 116 increasing the employers' contributions rate from 9.275% to 10.275% of employee compensation for fiscal year 2012, an additional 1% annually for each of the next four years, and 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective July 1, 2020. The purpose of this Act was to provide cash flow and strengthen the System to adequately cover administrative expenses and payment of benefits. The Municipality was required to contribute 11.275% of gross salary until the fiscal year ended on June 30, 2013. As stated in the Act, percent increases applicable to municipalities for fiscal years 2011-2012, 2012-2013 y 2013-2014 would be financed through the Commonwealth's budget approved by the Commonwealth's Legislature.

B. Act No. 3 of 2013 (beginning July 1, 2013)

In order to address its unfunded liability and rescue the System from insolvency, on April 4, 2013 the Commonwealth of Puerto Rico enacted Act No. 3 of 2013, representing a comprehensive reform of the ERS. Act No. 3 became effective on July 1, 2013 and amends the provisions of the different benefits structures under the ERS, including, but not limited to, the following:

- All participants (employees) under the defined benefit pension plans (Act 447 and Act 1) and the defined contribution plan (System 2000) were moved to a new hybrid plan ("New Plan").
- For active participants of the contributory defined benefit programs under Act No. 447 of 1951 and Act No. 1 of 1990, all retirement benefits accrued through June 30, 2013 were frozen. Thereafter, all future benefits will accrue under the New Plan. Participants will receive a pension at retirement age equivalent to what they had accrued under Act No. 447 and Act 1 up to June 30, 2013, and a supplemental annuity corresponding to contributions made after July 1, 2013.
- Participants under System 2000 will no longer receive a lump-sum payment upon retirement, but rather a lifetime annuity calculated at retirement based on a factor that will incorporate the individual's life expectancy and a rate of return.
- New participants under the New Plan will receive a lifetime annuity based on the accumulated balance of their individual accounts (employees' contributions plus a return on investment)
- Eliminated the possibility of accruing a merit pension (payable once the participant had achieved 30 years of creditable service) after June 30, 2013.
- Increased employee contributions from 8.275% to a minimum of 10.000%.
- After July 1, 2013 all employers must contribute 12.275% of employee contribution with an additional 1% annually up to June 30, 2016; after July 1, 2016 an additional 1.25% annually for each of the five years thereafter, reaching an aggregate contribution rate of 20.525% effective

12. PENSION PLAN (CONTINUED)

- July 1, 2020. These contributions will be used to increase the System’s assets, reduce the actuarial deficit and enable the System to comply with future obligations.
- Retirement age was modified as follows:
 - ✓ Act No. 447 regular employees: age 58 to 61,
 - ✓ Act No. 447 high risk employees (state and municipal police, firefighters and custody officials): from age 50 to 55 years,
 - ✓ Act No. 305 (System 2000) regular employees: age 60 to 65; high risk employees remains the same (55 years).

Act 1 employees remained the same (65 years for regular employees and 55 for high risk employees. For new employees under the New Plan will retire after 67 years (retirement age will be 67 for regular employees and 58 for high risk employees).

- Due to changes to Special Laws (see note 14), the minimum monthly pension for current retirees was increased from \$400 to \$500.
- Disability benefits were eliminated and substituted for a mandatory disability insurance policy. Beginning July 1, 2013, each employee must contribute to this insurance plan .25% of his or her monthly salary, up to a monthly maximum of \$5,000. Therefore, the maximum monthly employee contribution will be \$12.50 (\$5,000 x .25%).
- Survivor benefits were modified.

The Municipality’s actual contribution for the current and the previous two fiscal years, which is equal to the required contribution, follows:

<u>Fiscal year ended:</u>	<u>Law No. 3</u>
2014	<u>\$ 344,118</u>

A. Act No. 32 of 2013 (beginning July 1, 2013)

On June 25, 2013, Act No. 32 was approved in order to amend Act No. 447 of 1957 by creating a new Article 5-117 *Additional Uniform Contribution* (AUC), with the purpose of solving the cash flow deficit of the System. For each fiscal year, beginning on July 1, 2013, the ERS will: 1) determine the portion of the AUC attributable to each participating employer based on the percentage each employer’s contributions represent of the total employer contributions established for that fiscal year; and 2) send to the director of the P.R. Office of Management and Budget (OMB) and to each public corporation and municipality whose employees are covered by this Act, a certification of the AUC owed by each employer.

12. PENSION PLAN (CONTINUED)

Act No. 32 defines the concept of the AUC as follows:

- For the fiscal year 2013-2014, the AUC will be one hundred and forty million dollars (\$140,000,000).
- For each subsequent fiscal year, beginning with the 2014-2015 fiscal year until 2032-2033, the AUC will be the contribution certified by the external actuary of the System, at least 120 days prior to the beginning of each fiscal year, deemed necessary to prevent that the value of the System's projected gross assets, during any subsequent fiscal year, be lower than one thousand million dollars (\$1,000,000,000). If, for any fiscal, the certified AUD is not available within the 120-day period prior to the beginning of the said fiscal year or within a shorter term with the consent of the OMB, the AUC will be equal to the contribution certified for the immediate preceding fiscal year.

Each public corporation and municipality covered by this Act is directly responsible for the payment of their corresponding certified AUC. However, for any fiscal year, the OMB will consign in the Commonwealth's General Budget enough resources to subsidy totally or partially the AUC certified to any public corporation, municipality or governmental entity, including the Judiciary Branch, whose operating expenditures are not fully or partially covered by the General Budget and for which the OMB, has subsequently determined it does not have the financial capacity to assume such obligation during the fiscal year.

For the fiscal year 2013-2014, \$41.142 million dollars were assigned to OMB through Commonwealth Legislative Resolution of Special Assignments No. 17 (RC 17-2013) for the total or partial subsidy of the AUC of any public corporation or municipality that the agency determined did not have the financial capacity to assume this obligation. The OMB's evaluation of a municipality's financial capacity was based on two parameters: financial indicators and population. The financial indicators to be evaluated were: profitability index (net income as a percentage of revenues); capital ratio (the proportion between the net position of the entity and the AUC) and debt margin ratio (the proportion between the AUC and the municipality's special ad valorem tax debt margin (CAE)). For the fiscal year ended June 30, 2014, the AUC partially subsidy received by the Municipality from OMB was \$143,550, which equaled the total contribution required.

13. FUND BALANCE (DEFICIT)

As of June 30 2014, fund balance is comprised of the following:

<u>Fund Balance (Deficit)</u>	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Bond Issue</u>	<u>State Assignment</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Restricted for:						
General government	\$ -	\$ -	\$ -	\$ -	\$ 362,941	\$ 362,941
Public work			3,135,485	2,656,043	2,144,125	7,935,653
Public safety					18,100	18,100
Health and welfare					130,695	130,695
Culture and recreation					54,784	54,784
Education					90,568	90,568
Debt service		1,008,686				1,008,686
Unassigned	<u>(5,585,613)</u>					<u>(5,585,613)</u>
Total Fund Balance	<u>\$ (5,585,613)</u>	<u>\$ 1,008,686</u>	<u>\$ 3,135,485</u>	<u>\$ 2,656,043</u>	<u>\$ 2,801,213</u>	<u>\$ 4,015,814</u>

14. RISK MANAGEMENT

The Property Division of the Municipality is responsible of assuring that the Municipality's property is properly insured. Annually, the Property Division compiles the information of all property owned and its respective market value. After evaluating this information, the Property Division submits the data regarding the Municipality's properties to the Area of Public Insurance at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities. Settled claims have not exceeded commercial coverage in any of the past three fiscal years.

15. FUTURE ADOPTION OF ACCOUNTING PRONOUNCEMENTS

The GASB has issued the following statements, which the Municipality has not yet adopted:

1. **GASB Statement No. 68 "Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27."** The provisions of this Statement are effective for fiscal years beginning after June 15, 2014 (fiscal year ended June 30, 2015).
2. **GASB Statement No. 69 "Government Combinations and Disposals of Government Operations."** The provisions of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis (fiscal year ended June 30, 2015).
3. **GASB Statement No. 71 "Pension Transition for Contributions Made Subsequent to the Measurement Date."** The provisions of this Statement should be applied simultaneously with the provisions of Statement 68 (fiscal year ended June 30, 2015).

The impact of these statements on the Municipality's financial statements, if any, has not yet been determined.

16. PRIOR PERIOD ADJUSTMENTS

A. GOVERNMENTAL FUND FINANCIAL STATEMENTS

The following restatements have been made in the governmental fund financial statements, which are reported as an adjustment to the beginning fund balances:

<u>Description</u>	<u>General Fund</u>	<u>Bond Issue Fund</u>	<u>HUD Programs</u>	<u>Health and Human Services Grants</u>	<u>Homeland Security Grants</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Fund balance (deficit), beginning	\$ (7,727,477)	\$ 3,360,807	\$ 28,456	\$ -	\$ 506,361	\$ 1,275,898	\$ 4,466,449	\$ 1,910,494
<u>Correction of errors:</u>								
Understatement of accounts payable and accrued liabilities	(323,482)							(323,482)
Understatement of accounts receivables	22,361							22,361
To reclassified accounts payable and accrued liabilities	2,365,905							2,365,905
Overstatement of principal and interests payable						332,415		332,415
Fund balance, beginning as restated	\$ (5,662,693)	\$ 3,360,807	\$ 28,456	\$ -	\$ 506,361	\$ 1,608,313	\$ 4,466,449	\$ 4,307,693

16. PRIOR PERIOD ADJUSTMENTS (CONTINUED)

B. GOVERNMENTAL-WIDE FINANCIAL STATEMENTS

The following restatements have been made in the governmental-wide financial statements, which are reported as an adjustment to the beginning net position:

Description	Governmental Activities
Net position – beginning	\$ 14,357,848
Understatement of accounts payable and accrued liabilities	(323,482)
Understatement of accounts receivables	22,361
Overstatement of interests payable	15,415
Understatement of Christmas bonus accounts receivable	98,899
Understatement of Christmas bonus accounts payable	(212,930)
Understatement of accounts payable and accrued liabilities - Consolidate Waste	(768,947)
Net position – beginning, as restated	<u>\$ 13,189,164</u>

17. SUBSEQUENT EVENTS

A. Implementation of Acts No. 18 and 19 of 2014

The dispositions established by Acts 18 and 19 of 2014 related to the municipal sales and use tax became effective on July 1, 2014 (see note 3). The most significant changes are the creation of the Municipal Finance Corporation (COFIM) and, for the municipalities covered by these Acts, the new collection method of the 1% municipal sales and use tax and the establishment of a monthly advances system for the transfers of the .2% destined for the Municipal Development Fund (FDM) and of the .2% related to the Municipal Redemption Fund (FRM).

For those municipalities that signed the agreement to be covered by these Acts (including the Municipality of Vega Baja), the transfers to be made by the Governmental Development Bank (GDB) of the .2% destined for the FDM and of the .2% related to the FRM will be based on a system of monthly advances: each month the GDB will make the FDM and FRM transfers based on the amounts collected that same month in the preceding fiscal year (2013-2014). At the end of the year, a settlement will be made comparing the actual collections of the FDM and FRM with the monthly advances made to each municipality. If actual collections exceed the total advances received, an account receivable from GDB will be recognized; if actual collections are less than the total advances, a payable to the GDB will be recognized and amortized through withholdings from future advances. For municipalities not covered by these Acts, the monthly transfers will be made based on actual collections.

17. SUBSEQUENT EVENTS (CONTINUED)

As stated in Act 19, the 1% corresponding to the municipalities' sales and use tax will be deposited in COFIM. From these funds COFIM will deposit to the COFIM's sinking fund the greater of: .3% of the 1% municipal sales and use tax or an Annual Rental Fee (RFA). The RFA for fiscal year 2014-2015 will be \$65,541,281 and, thereafter, 1.5% of the RFA of the preceding fiscal period. The excess of the required deposit to the COFIM's sinking fund (.7% of the 1% of the municipal sales and use tax) will be transferred to the general fund of municipalities covered by the agreement or to the FRM as decided by the municipality. Before the transfer of the .7% to the municipalities covered by the Act, COFIM will transfer the 1% municipal sales and use tax to the municipalities not covered by the Act.

On September 1, 2014, the sixteen municipalities that collect their sales and use tax through the P.R. Department of Treasury (Aguadilla, Aibonito, Arroyo, Barranquitas, Ciales, Culebra, Hatillo, Juncos, Lajas, Lares, Maricao, Maunabo, Naguabo, Patillas, Peñuelas and Rincon) began participating on a pilot program for the collection of the 1% municipal sales and use tax through COFIM. In this program, a standard monthly sales and use tax return was created to be used by the retailers of these municipalities. The monthly returns were filed in the bank branches of the financial institution designated by COFIM to be its intermediary, the Popular Bank of Puerto Rico (BPPR). BPPR would electronically process the returns and submit their data to COFIM. However, beginning November 1, 2014, the retailers also had the option of using COFIM's internet portal to electronically file and pay the return.

On the other hand, the Governing Board of COFIM has not established an implementation date for the remaining 62 municipalities. However, for those municipalities that voluntarily decided to use COFIM's internet portal or collection process through the BPPR, their implementation date was December 1, 2014. For those municipalities that want to be certified as collection agents for COFIM, the implementation date was January 1, 2015. As collection agents for COFIM, the retailers of these municipalities have the option of filing and paying the monthly sales and use tax in the municipality's Collection Office. The Collection Office's personnel have the responsibility to deposit the daily sales and use tax collections in the bank account designated by COFIM, and also submit electronically the returns' data to the agency for processing in COFIM's data base. The Municipality of Guayama has been certified by COFIM as a collection agent and the implementation of the new collection system began on February 1, 2015.

	Budgeted Amount		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 1,193,147	\$ 1,193,147	\$ 1,193,147	\$ -
Municipal license tax	510,000	510,000	477,770	(32,230)
Construction excise taxes	510,965	510,965	190,593	(320,372)
Fines and forfeiture	15,000	15,000	6,080	(8,920)
Charges for services	63,000	63,000	51,886	(11,114)
Intergovernmental	6,882,203	6,882,203	7,049,384	167,181
Interest	50,000	50,000	4,498	(45,502)
Miscellaneous	1,907,527	1,907,527	557,542	(1,349,985)
Municipal sales and use tax	475,000	475,000	265,564	(209,436)
Total revenues	<u>11,606,842</u>	<u>11,606,842</u>	<u>9,796,464</u>	<u>(1,810,378)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER				
FINANCING USES:				
Current:				
General government	5,657,493	6,169,901	5,647,208	522,693
Public safety	1,083,514	1,014,091	962,290	51,801
Public works	3,247,469	2,739,339	2,300,708	438,631
Health and welfare	480,653	518,545	447,034	71,511
Culture and recreation	736,288	763,541	547,699	215,842
Operating transfer to other funds	401,425	401,425	376,735	24,690
Total expenditures, encumbrances and other financing uses	<u>11,606,842</u>	<u>11,606,842</u>	<u>10,281,674</u>	<u>1,325,168</u>
EXCESS (DEFICIENCY) OF REVENUES UNDER)EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)			<u>(485,210)</u>	<u>(485,210)</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 9,796,464
Differences-budget to GAAP:				
GAAP adjustments to revenues				<u>24,614</u>
Total revenues and other financing sources as reported in the statement of revenues, expenditures, and changes in fund balances				<u>\$ 9,821,078</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 10,281,674
Differences-budget to GAAP:				
Encumbrances for supplies and equipment ordered, but not received, are reported in the year the order is placed for budgetary reporting purposes				(183,444)
Transfer to other funds are outflows of budgetary resources but are not expenditures for financial reporting purposes				(376,735)
GAAP adjustments to expenditures				<u>696,793</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 10,418,288</u>

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

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

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2014 representing the Municipality's original budget. There were no supplemental appropriations for the year ended June 30, 2014.

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
<u>U.S. DEPARTMENT OF AGRICULTURE:</u>			
Pass-through Commonwealth of Puerto Rico Department of Education: Child and Adult Care Food Program	10.558	Not Available	\$ 66,012
Total U.S. Department of Agriculture			66,012
<u>U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:</u>			
Direct Program: Section 8 - Housing Choice Voucher	14.871	N/A	322,370
Pass-through: Commonwealth of Puerto Rico – Commissioner Office of Municipal Affairs Community Development Block Grants (State Program)	14.218	Not Available	612,085
Total U.S. Department of Housing and Urban Development			934,455
<u>U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:</u>			
Direct Program: Head Start	93.600	N/A	991,272
Pass-through the Commonwealth of Puerto Rico – Family Department (ACUDEN): Child Care and Development Block Grant	93.575	Not Available	29,259
Total U.S. Department of Health and Human Services			1,020,531
<u>U.S. DEPARTMENT OF HOMELAND SECURITY:</u>			
Public Assistance Grant Pass-through the Commonwealth of Puerto Rico Governors: Authorized Representative to FEMA (GAR) Disaster Grant Public Assistance	97.036	Not Available	273,167
Total U.S. Department of Homeland Security			273,167
TOTAL EXPENDITURES OF FEDERAL AWARDS			\$ 2,294,165

1. BASIS OF PRESENTATION:

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

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the HUD Programs Fund, Health and Human Services Grants, Homeland Security Grants and Other Governmental Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the funds financial statements and the disbursements in the Schedule of Expenditures of Federal Awards is as follows:

<u>Description</u>	<u>Other Governmental Funds</u>
Per Schedule of Expenditures of Federal Awards	\$ 2,294,165
Additional amount recorded as expenditures under modified accrual- basis for Section 8 HCV Program	157,158
Non federal programs Expenditures and transfer out	<u>5,636</u>
Total expenditures in the basic financial statements	<u><u>\$ 2,456,959</u></u>



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

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

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the **Municipality of Patillas**, Puerto Rico, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated June 26, 2015.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the **Municipality of Patillas'** internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the **Municipality of Patillas'** internal control. Accordingly, we do not express an opinion on the effectiveness of the **Municipality of Patillas'** internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questions costs as item **2014-001 thru 2014-005** to be material weaknesses.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the **Municipality of Patillas'** financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items **2014-001** thru **2014-008**.

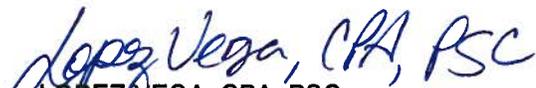
We noted certain matters that we reported to management of the **Municipality of Patillas'** in a separate letter dated June 26, 2015.

Municipality of Patillas' Response to Findings

The **Municipality of Patillas'** response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. **Municipality of Patillas'** response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited.


LOPEZVEGA, CPA, PSC

San Juan, Puerto Rico
June 26, 2015

Stamp No. 2705476 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



López-Vega, CPA, PSC

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

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

Report on Compliance for Each Major Federal Program

We have audited the **Municipality of Patillas'** compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of **Municipality of Patillas'** major federal programs for the year ended June 30, 2014. **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.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of **Municipality of Patillas'** major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *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 we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **Municipality of Patillas'** compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the **Municipality of Patillas'** compliance.

Basis for Qualified Opinion on Community Development Block Grants – State's Program

As described in the accompanying schedule of findings and questioned costs, the **Municipality of Patillas'** did not comply with requirement regarding CFDA No. 14.228 Community Development Block grants – State's Program as described in findings numbers **14-006** and **14-007** for *activities allowed (housekeeper and housing rehabilitation)* and **14-008** for *real property management*. Compliance with such requirements is necessary, in our opinion, for **Municipality of Patillas'** to comply with the requirements applicable to that program.

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133 (CONTINUED)

Qualified Opinion on Community Development Block Grants – State's Program

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the **Municipality of Patillas'** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

Unmodified Opinion on Each of the Other Major Federal Programs

In our opinion, the **Municipality of Patillas** complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its other major federal programs identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs for the year ended June 30, 2014.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items **14-006** thru **14-014**. Our opinion on each major federal program is not modified with respect to these matters.

The Municipality of Patillas' response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The **Municipality of Patillas'** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control over Compliance

Management of **Municipality of Patillas'** is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the **Municipality of Patillas'** internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of **Municipality of Patillas'** internal control over compliance.



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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133 (CONTINUED)

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items **2014-006**, **2014-007** and **14-008** to be material weaknesses.

A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned cost as items; **2014-009** thru **2014-014** to be significant deficiencies.

Municipality of Patillas' response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. **Municipality of Patillas'** response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

We noted certain matters that we reported to management of the **Municipality of Patillas'** in a separate letter dated June 26, 2015.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
June 26, 2015

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Section I – Summary of Auditor’s Results

Financial Statements

Type of auditor’s report issued: **Qualified for Fund Financial Statements and Adverse for Government-wide Financial Statements**

Internal control over financial reporting:

Material weakness identified? Yes No

Significant deficiencies identified not considered to be material weaknesses? Yes No

Noncompliance material to financial statements noted? Yes No

Federal awards

Internal Control over major programs:

Material weakness identified? Yes No

Significant deficiencies identified not considered to be material weaknesses? Yes No

Type of auditor’s report issued on compliance for major programs: **Unmodified, except for qualified for Community Development Block Grant – State’s Program (14.228)**

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

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grant – State’s Program
14.871	Section 8 Housing Choice Voucher
93.600	Head Start Program
97.036	Disaster Grant Public Assistance

Dollar threshold used to distinguish between Type A and Type B programs \$ 300,000

Auditee qualified as low-risk auditee? Yes No

Section II – Financial Statements Findings

(The following findings are considered significant deficiencies or material weakness. Those that are material weaknesses are labeled as (MW)).

Finding Reference	2014-001
Requirement	Operating deficit of general fund (MW)
Statement of Condition	The Municipality closed its fiscal year ended on June 30, 2014 with a fund balance deficiency in the general fund of (\$5,585,613).
Criteria	Article 8.004(b) of the Municipalities Law establishes the Municipality cannot obligate or spend funds in excess of the ongoing fiscal year. No amount shall be expended or obligated in a given fiscal year in excess budgeted or authorized amounts by the Municipal Legislature.
Cause of Condition	The overstatement of estimated revenues accounts in prior years caused that the Municipality operated with a deficit.
Effect of Condition	The continued occurrence of this situation may result in possible significant fund limitations and eventual reduction or elimination of municipal services since future revenues will need to be used to pay for accumulated liabilities.
Recommendation	We recommended management to evaluate the adequacy of the provision for deficit reserve accounts in the next budget. Also, the Municipality’s officers must evaluate the trend in the negative variance between budgeted revenues and actual revenues to reduce the budgeted expenditures by department (quarterly allocation process) and to avoid future operational deficits at year-end.
Questioned Costs	None
Management Response and Corrective Action	The Municipality have taken aggressive action to increase revenues and has implemented more efficient control over expenditures to reduce and, in a near future, eliminate the accumulated deficit and prevent future budget deficits. In addition, the Municipality restructured its debt and increase the efficiency in administration operations by transforming procurement from a tactical, transaction-oriented function into a strategic one.

Implementation Date: Still in process

Responsible Person: Sra. Lianette León – Finance Director

Section II – Financial Statements Findings

Finding Reference	2014-002
Requirement	Accounting Records and Reporting System (MW)
Statement of Condition	<p>During our examination of the accounting cycle, we noted that the Municipality did not maintain an accounting system that generates accurate accounting information for the preparation of the financial statements in conformity with generally accepted accounting principles (GAAP).</p> <p>The Municipality’s accounting records are maintained in a cash and budgetary basis and at the end year, personnel of the Finance Department and external consultants summarized in electronic worksheets the revenues, expenditures, encumbrances, capital assets transactions, accounts receivables, accounts payable and long-term debts. These worksheets are used for the preparation of the financial statements.</p>
Criteria	<p>Chapter VIII, Article 8.010 (b) of State Act Number 81 – “<i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico</i>” of 30 August 30, 1991, states that the Municipality must maintain its fund accounting in accordance with GAAP. In addition, Article 8.010 (c) states that uniform accounting systems used by the Municipality must produce reliable reports and financial statements provide complete information about the results of the Municipality’s operations and include the necessary internal controls to account for all funds, capital assets and other assets.</p>
Cause of Condition	<p>The Municipality has not established effective internal control procedures over the preparation of the financial statements and the transactions recorded on its accounting records.</p>
Effect of Condition	<p>The Municipality is not in compliance with Chapter VIII, Articles 8.010 (b) and (c) of the State Law Number 81 of August 30, 1991.</p>
Recommendation	<p>We recommend management to establish the necessary internal controls and procedures in order to maintain a complete accounting system that provides for the preparation of financial statements in accordance with GAAP.</p>
Questioned Cost	None

Section II – Financial Statements Findings

Finding Reference **2014-002 (continued)**

**Management Response
and Corrective Action**

The Municipality's management, during the fiscal year 2014-2015, initiated the implementation of a new accounting software that will provide the maintenance a complete accounting records. The financial data processed in this system should provide for the preparation of financial statements, in accordance with GAAP.

Implementation Date: Still in process

Responsible Person: Sra. Lianette León – Finance Department Director

Section II – Financial Statements Findings

Finding Reference	2014-003
Requirement	Accounting Records – Interfund Transactions (MW)
Statement of Condition	<p>The Municipality does not maintain an accurate record over the special revenue funds transactions and the interfund transactions of Municipal funds.</p> <p>During our examination of the accounting records, we noted that the Municipality does not maintain adequate subsidiary records to accurately account for interfund balances, presented in the Balance Sheet, for the fiscal year 2013-2014. This situation caused that monies of the general fund and various special revenue funds were used as loans, to pay operational costs of other funds.</p>
Criteria	<p>Article 8.004 (c) of the State law Number 81 – <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico de 1991</i> – August 30, 1991, states that the restricted funds received by the Municipality should be only used for the purposes established by these resources. In addition, Article 8.010 (c) (2) and (3) of State Act Number 81 stated that the Municipality should maintain accurate accounting records and funds controls.</p>
Cause of Condition	<p>The Municipality did not maintain an adequate control of the accountability of the interfund transactions and the due from and due to account balances.</p>
Effect of Condition	<p>The Municipality is not in compliance with Chapter VIII, Article 8.004 (c) and Article 8.010 (c) (2) (3) of the State Act No. 81.</p>
Recommendation	<p>We recommend management to implement procedures in order to obtain and maintain all the required documentation regarding the interfund transactions.</p>
Questioned Cost	None
Management Response and Corrective Action	<p>As part of our corrective action plan, we will identify the origin of all Municipality’s interfund transactions, in order to make the necessary adjustments to correct any discrepancies identified. In addition, we will implement accounting records to account for such transactions.</p>

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Sra. Lianette León – Finance Department Director

Section II – Financial Statements Findings

Finding Reference	2014-004
Requirement	Capital Assets and Expenditures – Subsidiary Ledger (MW)
Statement of Condition	The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net position, and expenses of the governmental activities is not determinable.
Criteria	Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain updated property accounting records. Also, the GASB Statement No. 34 requires that all capital assets, including infrastructure, must be presented in the Statement of Net Position and that these assets must be depreciated during its useful life.
Cause of Condition	Competent and sufficient evidential matter related to the capital assets was not available to support the value, completeness and ownership of these assets.
Effect of Condition	The Municipality's Government-Wide Financial Statements does not present fairly, the financial position of the governmental activities, and the change in financial position of the Municipality.
Recommendation	We recommend that the Municipality should continue the compilation of documents to support the value, completeness and ownership of its capital assets, necessary to comply with the requirements of the GASB Statement No. 34.
Questioned Cost	None
Management Response and Corrective Action	The Municipality's Finance Department staff plans to continue in their effort to update the capital assets subsidiary ledger, principally the construction in progress and infrastructure assets.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Sra. Lianette León – Finance Department Director

Section II – Financial Statements Findings

Finding Reference **2014-005**

Requirement **Municipal license tax revenues (MW)**

Statement of Condition Municipal license tax revenues of the fiscal year 2014-2015, which were collected in advance from taxpayers between January 1 thru June 30, 2014 (known in Spanish as "Patente en Suspenso"), were used by the Municipality to cover certain operating costs and cash flows shortages of the general fund during the fiscal year ended June 30, 2014. Those unearned revenues collected in advance pertain to the general fund's operating budget of the fiscal year 2014-2015, and must not be used to pay obligations of the prior year.

Criteria Article 8.004(b) of Law No. 81 of August 30, 1991, known as the Autonomous Municipalities Act of Puerto Rico (Law No. 81) states that the Municipality cannot use or obligate any amount in a given fiscal year that exceeds the appropriations and the resources authorized by ordinance or resolution for such fiscal year. In addition, the Municipality cannot be committed, in any form, to any contract or negotiation for the future payment of amounts that exceed the current fiscal year's budgeted resources.

Cause of Condition The foregoing condition is primarily due to the facts that the Municipality does not prepare cash flows forecasts and projections to anticipate any cash flows shortage. Management does not have timely and accurate information regarding its operations and cannot monitor the adherence to the established budget appropriations and cash flows.

Effect of Condition This situation will result in possible significant general fund limitations and eventual reduction or elimination of municipal services since future revenues were used to pay for accumulated liabilities.

Recommendation We recommend the Municipality to prepare cash flows forecasts and projections to anticipate any cash flows shortages and to avoid using financial resources of future fiscal years to cover the operating needs of the current fiscal year.

Questioned Costs None

Management Response and Corrective Action With the implementation of the corrective actions taken to the Finding 13-01, we expect to avoid or, at least, reduce the use of the municipal license tax revenues collected in advance, in future fiscal years.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Sra. Lianette León – Finance Department Director

Section III – Major Federal Award Program Findings and Questioned Costs

(The following findings are considered significant deficiencies or material weakness. Those that are material weaknesses are labeled as (MW)).

Finding Reference	2014-006
Program	Community Development Block Grants – State’s Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass-through the Commonwealth of Puerto Rico – Office of the Commissioner for Municipal Affairs (OCAM)
Requirement	Activities Allowed – Housekeeper Activities (MW)
Statement of Condition	<p>We performed a housekeeper activities test of ten (10) participant’s files and we noted that the Municipality did not maintain complete and updated participants’ files as required by the Operational Guide for the Housekeeper Services. In our tests we found the following exceptions:</p> <ul style="list-style-type: none"> a) In four (4) participants’ files, the application form (Form OCAM-AH-002) was not completed by the participant prior to be selected by the Municipality to receive CDBG Program benefits. b) In four (4) participants’ files, evidence of the approval or denial letter sent to the applicant was not in file (OCAM-AH-004-A or OCAM-AH-004-B). c) In ten (10) participants’ files, we did not find evidence that demonstrate if the program staff visited at least two (2) times per month the participant housing unit to ensure the quality of services. d) In four (4) cases, the Services Coordinator (Municipal Employee) did not complete the Form OCAM-AH-006 to evaluate the housekeeper performance when visited the participant housing unit.
Criteria	<p>24 CFR Section 570.482 Eligible Activities, (f) <i>Standards for evaluating public benefit</i>, (6) <i>Documentation</i>, establishes that the state and its grant recipients must maintain sufficient records to demonstrate the level of public benefit, based on the above standards, that is actually achieved upon completion of the CDBG-assisted economic development activities and how that compares to the level of such benefit anticipated when the CDBG assistance was obligated. If a state grant recipient’s actual results show a pattern of substantial variation from anticipated results, the state and its recipient are expected to take those actions reasonably within their respective control to improve the accuracy of the projections.</p>

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **2014-006 (Continued)**

Criteria(continued) If the actual results demonstrate that the state has failed the public benefit standards, HUD may require the state to meet more stringent standards in future years as appropriate.

Cause of Condition The Municipality’s controls and procedures failed to assure that the participants’ files include all the required documents to comply with the program requirements.

Effect of Condition The Municipality is not in compliance with the Code of Federal Regulations 24, Section 570.482 and with the operational guide.

Recommendation We recommended management to follow the procedures established by the Office of the Commissioner of Municipal Affairs (OCAM) in the procedures manual, including the use of the forms included on it.

Questioned Costs None

Management Response and Corrective Action The Program’s staff with the responsibilities to maintain the participants’ files in compliance with the Program regulations was required to take corrective measures in order to ensure application of all of the procedures and to use all forms specified in the procedures guide “Guía Operacional para la Prestación del Servicio de Auxiliares en el Hogar”. Also, the Program staff will be monitored frequently for compliance, by the Federal Programs Department Director

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Ms. Wilma Lugo
Federal Programs Director

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	2014-007
Program	Community Development Block Grants – State’s Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass-through the Commonwealth of Puerto Rico – Office of the Commissioner for Municipal Affairs (OCAM)
Requirement	Activities Allowed - Housing Rehabilitation (MW)
Statement of Condition	During our examination of Housing Rehabilitation Program we found that the Municipality did not maintain participant’s files in order to obtain sufficient, competent evidential matter with respect to the Program operations in this activity.
Criteria	24 CFR Section 570.506, each recipient shall establish and maintain sufficient records to enable the Secretary to determine whether the recipient has met the requirements of this part. At a minimum, the following records are needed: (a) Records providing a full description of each activity assisted (or being assisted) with CDBG funds, including its location (if the activity has a geographical locus), the amount of CDBG funds budgeted, obligated and expended for the activity, and the provision in subpart C under which it is eligible. (9) For each residential rehabilitation activity determined to aid in the prevention or elimination of slums or blight in a slum or blighted area: (i) The local definition of “substandard”; (ii) A pre-rehabilitation inspection report describing the deficiencies in each structure to be rehabilitated; and (iii) Details and scope of CDBG assisted rehabilitation, by structure. (10) For each activity determined to aid in the prevention or elimination of slums or blight based on the elimination of specific conditions of blight or physical decay not located in a slum or blighted area: (i) A description of the specific condition of blight or physical decay treated; and (ii) For rehabilitation carried out under this category, a description of the specific conditions detrimental to public health and safety which were identified and the details and scope of the CDBG assisted rehabilitation by structure.
Cause of Condition	The program has not established adequate internal control procedures to assure that rehabilitations are duly completed as required by regulations and appropriate documentation is maintained.
Effect of Condition	The Municipality is not in compliance with 24 CFR, Section 570.506.
Recommendation	We recommend the Program to maintain sufficient records to enable the pertinent agencies to determine whether the recipient has met the requirements established in 24 CFR section 570.506.

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 2014-007 (Continued)

Questioned Costs None

**Management Response
and Corrective Action**

The Municipality's Management concurs with the finding. The Federal Office Director will establish communication with the program staff in order to strengthen its program procedures to ensure the Municipality be in compliance with the activities related with Housing Rehabilitation.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Ms. Wilma Lugo
Federal Program Director

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 2014-008

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

Requirement **Equipment and Real Property Management (MW)**

Statement of Condition **Section II – Financial Statements Findings – Finding Reference 2014-004**

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	2014-009
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871); U.S. Department of Housing and Urban Development
Requirement	Eligibility – Eligibility for Individuals
Statement of Condition	<p>During our Eligibility Test, we examined twenty (20) participant's files and we noted the following situations:</p> <ul style="list-style-type: none">a. In eleven (11) cases the Enterprises Income Verification (EIV) was not performed.b. In nine (9) cases, the EIV Reports were not signed by the participants.
Criteria	<p>24 CFR Part 5, Subpart B, section 5.233 (2) Processing entities must use HUD's EIV system in its entirety: (i) As a third party source to verify tenant employment and income information during mandatory reexaminations or re-certifications of family composition and income, in accordance with §5.236, and administrative guidance issued by HUD; and (ii) To reduce administrative and subsidy payment errors in accordance with HUD administrative guidance. (b) Penalties for noncompliance. Failure to use the EIV system in its entirety may result in the imposition of sanctions and/or the assessment of disallowed costs associated with any resulting incorrect subsidy or tenant rent calculations, or both. On the other hand, 24 CFR, Part 5, Subpart B, section 5.212, Compliance with the Privacy Act and other requirements, (a) Compliance with the Privacy Act. The collection, maintenance, use, and dissemination of SSNs, EINs, any information derived from SSNs and Employer Identification Numbers (EINs), and income information under this subpart shall be conducted, to the extent applicable, in compliance with the Privacy Act (5 U.S.C. 552a) and all other provisions of Federal, State, and local law. (b) Privacy Act notice. All assistance applicants shall be provided with a Privacy Act notice at the time of application. All participants shall be provided with a Privacy Act notice at each annual income recertification.</p>
Cause of Condition	<p>The Program's officers did not complete the required documentation to validate the participant's eligibility. In addition, the Municipality did not follow what is established in 24 CFR 5.233 and 5.212</p>
Effect of Condition	<p>The Program does not meet all in compliance with Code of Federal Regulations 24, Sections 5.233 and 5.212, and could have an effect in the performance on SEMAP report.</p>

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **2014-009 (Continued)**

Recommendation The Program should strengthen internal control procedures to ensure compliance with its compliance requirements and train staff on documentation and verification process.

Questioned Costs None

**Management Response
and Corrective Action**

The Municipality's management concurs with the finding. During this fiscal year 2014-2015, the Program's staff will be working to correct the situations detailed in the finding.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Ms. Wilma Lugo
Federal Program Director

Section III – Major Federal Program Award Findings and Questioned Costs

Finding Reference	2014-010
Program	Section 8 Housing Choice Vouchers (CFDA. No. 14.871); U.S. Department of Housing and Urban Development
Requirement	Reporting – Financial Reporting
Statement of Condition	We performed a reporting test and noted that the audited financial data for the fiscal year 2013-2014 (submitted electronically) was not submitted to HUD through the Real Estate Assessment Center (REAC) in the stipulated time.
Criteria	24 CFR section 5.801 (b) <i>Submission of financial information</i> . Entities to which this subpart is applicable must provide to HUD, on an annual basis, such financial information as required by HUD. This financial information must be: (1) Prepared in accordance with Generally Accepted Accounting Principles as further defined by HUD in supplementary guidance; (2) Submitted electronically to HUD through the internet, or in such other electronic format designated by HUD, or in such non-electronic format as HUD may allow if the burden or cost of electronic reporting is determined by HUD to be excessive; and (3) Submitted in such form and substance as prescribed by HUD. (d) <i>Reporting compliance dates</i> . (1) for PHAs listed in paragraphs (a)(1) and (a)(2) of this section, the requirements of this section will begin with those PHAs with fiscal years ending September 30, 1999 and later. Unaudited financial statements will be required 60 days after the PHA's fiscal year end, and audited financial statements will then be required no later than 9 months after PHA's fiscal year end, in accordance with Single Audit and OMB Circular A-133 (24 CFR 84.26).
Cause of Condition	The Program did not submit timely the audited financial data as required by 24 CFR section 5.801 and by HUD.
Effect of Condition	The PHA is not in compliance with 24 CFR 5.801 and as prescribed by HUD.
Recommendation	Procedures should be implemented to ascertain that the PHA complies with the established Federal Regulation and as prescribed by HUD.
Questioned Costs	None

Section III – Major Federal Program Award Findings and Questioned Costs

Finding Reference **2014-010 (Continued)**

Management Response

and Corrective Action The Municipality management agrees with the finding. The Municipality's Management instructs the program accountant to submit timely GAAP-based audited financial information electronically to HUD once the Single Audit Report package is available.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Ms. Wilma Lugo
Federal Program Director

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	2014-011
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Housing Assistance Payment (HAP)
Statement of Condition	During our examination, we noted that the Section 8 Housing Choice Vouchers Program did not maintain a HAP register in the form required by HUD. The PHA is required to maintain a HAP contract register or similar record that must provide information as to the name and address of the family, the name and address of the owner, dwelling unit size, the beginning date of the lease term, the monthly rent payable to the owner, monthly rent payable by the family to the owner, and the monthly HAP. The record shall also provide data as to the date the family vacates and the number of days the unit is vacant if any.
Criteria	24 CFR Subpart D, Section 982.158 states (a) The PHA must maintain complete and accurate accounts and other records for the program in accordance with HUD requirements, in a manner that permits a speedy and effective audit. The records must be in the form required by HUD, including requirements governing computerized or electronic forms of record-keeping.
Cause of Condition	The Program is not performing an effective review of compliance requirements that are required by HUD and is not maintaining all the records required for the program.
Effect of Condition	The PHA is not in compliance with Code of Federal Regulations 24, section 982.158.
Recommendation	Procedures should be implemented to ascertain that the PHA complies with the established Federal Regulation, as prescribed by HUD.
Questioned Costs	None
Management Response and Corrective Action	The Municipality's management assigned a staff to the Program's accountant in order to maintain updated records, including HAP Register.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Ms. Wilma Lugo
Federal Program Director

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	2014-012
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871); U.S. Department of Housing and Urban Development
Requirement	Special Test – Utility Allowance Schedule
Statement of Condition	The PHA did not maintain an up-to-date utility allowance schedule for the audit period ended June 30, 2014. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten (10) percent or more in the utility rate.
Criteria	Code of Federal Regulations 24, Subpart K, Section 982.517 states that the PHA must maintain an up-to-date utility allowance schedule. The PHA must review utility rate data for each utility category on a yearly basis and must adjust its allowance schedule if there has been a rate change of ten percent or more for a utility category or fuel type since the last time utility allowance was revised.
Cause of Condition	The PHA did not follow the procedures established to review utility rate date each year.
Effect of Condition	The PHA is not in compliance with the Code of Federal Regulations 24, Subpart K, and Section 982.517.
Recommendation	The PHA should evaluate utility allowance rate each year as established in the federal regulations.
Questioned Costs	None.
Management Response and Corrective Action	To correct the condition reported by the external auditors, we will review the utility rate data for each category in order to determine any adjustment necessary to the utility allowance in use.

Implementation Date: Fiscal Year 2015-2016

Responsible Person: Ms. Wilma Lugo
Federal Program Director

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	2014-013
Program	Section 8 Housing Choice Vouchers Program (CFDA 14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Housing Quality Standards Inspections and HQS Enforcement
Statement of Condition	During our examination, the Municipality did not perform the required Housing Quality Control re-inspections during the fiscal year 2013-2014.
Criteria	Code of Federal Regulations 24, Subpart I, 982.404 and Section 982.158 (d) and 982.405 (b) states that the PHA must inspect the unit leased to a family at least annually to determine if the unit meets Housing Quality Standards (HQS) and the PHA must conduct quality control re-inspections. Also the PHA must prepare a unit inspection report.
Cause of Condition	The Municipality did not maintain adequate monitoring procedures to ensure that annual Housing Quality Control re-inspections are properly performed.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Section 982.404 and 982.158 (d) and 982.405 (b).
Recommendation	We recommend management to implement internal control procedures to ensure that annual inspections and quality control re-inspections are properly performed. The PHA supervisor or other qualified person must re-inspect a sample of units under contract during the last PHA fiscal year. Completed HQS inspections included in the sample must be no older than three months at the time of re-inspection. In addition, the quality control re-inspection should provide feedback on inspector's work, which can be used to determine if individual performance or general HQS training issues need to be addressed.
Questioned Costs	None
Management Response and Corrective Action	The Quality Control Re-inspections will be performed in accordance with our Administrative Plan, revised on March 2014. Implementation Date: Fiscal Year 2015-2016 Responsible Person: Ms. Wilma Lugo Federal Program Director

Section III – Federal Award Findings and Questioned Costs

Finding Reference	2014-014
Requirement	Single Audit Act
Statement of Condition	The Single Audit Report for the fiscal year ended June 30, 2014, was not issued within nine (9) months after the end of the audit period.
Criteria	The Single Audit Act of 1984, as amended, require that the audit report must be submitted to the Federal Audit Clearinghouse no later than nine (9) months after the end of the audit period.
Cause of Condition	The Municipality did not comply with the established regulation as prescribed in OMB Circular A-133.
Effect of Condition	The Municipality could lose federal grants since the noncompliance with Act requirements.
Recommendation	Procedures should be implemented to ascertain that the Municipality complies with the established Federal Regulation, as prescribed by OMB Circular A-133.
Questioned Costs	None
Management Response and Corrective Action	<p>We concur with this finding. The Municipality will establish a Financial Reporting Task Force composed of the management team of the Department of Finance and external consultants. We expect that the Single Audit reporting package for the fiscal year ended on June 30, 2014 will be completed on or before March 31, 2015.</p> <p>Implementation Date: Fiscal Year 2015-2016</p> <p>Responsible Person: Ms. Wilma Lugo Federal Program Director</p> <p>Ms. Lianette León Finance Department Director</p>

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
13-06	14.228	<p><u>We performed a housekeeper activities test of ten (10) participant's files and we noted that the Municipality did not maintain complete and updated participants' files as required by the Operational Guide for the Housekeeper Services. In our tests we found the following exceptions: a) In six (6) participant's files, the application form (Form OCAM-AH-002) was not completed by the participant prior to be selected by the Municipality to receive CDBG Program benefits. b) In seven (7) participant's files, the eligibility determination form was not completed by the program staff. c) In ten (10) participant's files, evidence of the approval or denial letter sent to the applicant was not in file (OCAM-AH-004-A or OCAM-AH-004-B). d) In ten (10) cases, the Services Coordinator (Municipal Employee) did not perform the required monthly visits to the participant housing unit with the purpose of inspect the quality of services provided by the housekeeper. e) In six (6) cases, the Services Coordinator (Municipal Employee) did not complete the Form OCAM-AH-006 to evaluate the housekeeper performance when visited the participant housing unit.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-006.</p>
13-07	14.228	<p><u>During our examination of Housing Rehabilitation Program we found that the Municipality did not maintain participant's files in order to obtain sufficient, competent evidential matter with respect to the Program operations in this activity.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-007.</p>
13-08	14.228	<p><u>During our Cash Management test, we examined twenty five (25) cash advances received by the program during the fiscal year 2012-2013 and we found that in fifteen (15) requisitions of funds (a total of \$44,510), the Municipality made the disbursements between twenty (20) to eighty six (86) days after the deposits.</u></p> <p>Corrective action was taken.</p>

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
13-09	14.228	<p><u>Equipment and Real Property Management (MW), Section II – Financial Statements Findings.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-008.</p>
13-10	14.871	<p><u>During our Eligibility Test, we examined fifteen (15) participant’s files and we noted the following situations: a) In five (5) cases the Enterprises Income Verification (EIV) was not performed. B)In two (2) cases, other members of the family did not complete the "Privacy Act Notice" corresponding to the annual income recertification.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-009.</p>
13-11	14.871	<p><u>We performed a reporting test and noted that the audited financial data for the fiscal years 2011-2012 and 2012-2013 (submitted electronically) were not submitted to HUD through the Real Estate Assessment Center (REAC) in the stipulated time.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-010.</p>
13-12	14.871	<p><u>During our examination, we noted that the Section 8 Housing Choice Vouchers Program did not maintain a HAP register in the form required by HUD. The PHA is required to maintain a HAP contract register or similar record that must provide information as to the name and address of the family, the name and address of the owner, dwelling unit size, the beginning date of the lease term, the monthly rent payable to the owner, monthly rent payable by the family to the owner, and the monthly HAP. The record shall also provide data as to the date the family vacates and the number of days the unit is vacant if any.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-011.</p>

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
13-13	14.871	<p><u>The PHA did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2013. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten (10) percent or more in the utility rate</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-012.</p>
13-14	97.036	<p><u>During our examination, the fiscal year Quarterly Reports (Fiscal Year 2012-2013) – Percentage of Completion Reports were not available for our examination.</u></p> <p>Corrective action was taken.</p>
13-15	N/A	<p><u>The Single Audit Report for the fiscal year ended June 30, 2013, was not issued within nine (9) months after the end of the audit period.</u></p> <p>No corrective action was taken. The auditors reissued the finding for the current year. Finding Reference 2014-014.</p>
12-02	97.036	<p><u>During a Cash Management test the Municipality’s financial management system did not 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 the audit that Municipality held cash balances over \$5,000 for periods longer than 3 days.</u></p> <p>Corrective action was taken.</p>

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
11-02	97.036	<p><u>During a Cash Management test the Municipality's financial management system did not 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 the audit that Municipality held cash balances over \$5,000 for periods longer than 3 days.</u></p> <p>The audit finding does not warrant further action because two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.</p>