

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES

AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE PEÑUELAS

AUDITORIA 2001-02

30 DE JUNIO DE 2002

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UNIDAD DE CORREO

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PEÑUELAS

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2002

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PEÑUELAS

YEAR ENDED JUNE 30, 2002

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PEÑUELAS

YEAR ENDED JUNE 30, 2002

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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 Peñuelas
Peñuelas, Puerto Rico**

We have audited the accompanying general-purpose financial statements of the **Municipality of Peñuelas**, as of and for the year ended June 30, 2002, as listed in the table of contents. These general purpose financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these general-purpose financial statements based on our audit.

Except as discussed in the following paragraph, we conducted our audit 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 the provisions of the Office of Management and Budget 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 the general-purpose financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the general-purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall general-purpose financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

The **Municipality of Peñuelas** accounting system and subsidiary records of property and equipment did not provide us sufficient competent evidence with respect to the amounts presented in the accompanying general-purpose financial statements. Therefore, we do not express an opinion on such amounts included in the general fixed assets account group.

In our opinion, except for the effect of such adjustments, if any, as might have been determined to be necessary had we been able to audit the general fixed assets account group, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of the **Municipality of Peñuelas** as of June 30, 2002, and the results of its operations for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITORS' REPORT- (CONTINUED)

In accordance with *Government Auditing Standards*, we have also issued our report dated November 27, 2002 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 grants.

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


LOPEZ- VEGA, CPA, PSC

San Juan, Puerto Rico
November 27, 2002

Stamp No. 1853989 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS
COMBINED BALANCE SHEET
ALL GOVERNMENTAL FUND TYPES AND ACCOUNT GROUPS
JUNE 30, 2002**

	GOVERNMENTAL FUND TYPES				ACCOUNT GROUPS		TOTALS (MEMORANDUM ONLY)
	General	Special Revenue	Debt Service	Capital Projects	General Fixed Assets	General Long-term Debt	
ASSETS AND OTHER DEBITS							
Cash	\$77,777	\$2,360,464		\$1,176,543			\$3,614,784
Cash with fiscal agent	67,392	7,418	\$1,404,625	3,344,828			4,824,263
Intergovernmental receivables	445,250	112,341					557,591
Municipal license taxes receivable	7,619						7,619
Federal grants receivable		174,500					174,500
Due from other funds	626,632						626,632
Other receivables	14,439						14,439
Property and equipment					\$15,473,223		15,473,223
Amount available in Debt Service Fund						\$1,404,625	1,404,625
Amount to be provided for retirement of general long-term debt						21,323,925	21,323,925
Total assets and other debits	\$1,239,109	\$2,654,723	\$1,404,625	\$4,521,371	\$15,473,223	\$22,728,550	\$48,021,601
LIABILITIES AND FUND EQUITY							
Liabilities:							
Accounts payable and accrued liabilities	\$368,714	\$232,044					\$600,758
Due to other funds		562,095		\$64,537			626,632
Due to other governmental entities	9,213	309,132				\$9,703,935	10,022,280
Deferred municipal license tax revenues	2,108,931						2,108,931
Deferred federal grant revenues		700,093					700,093
General obligation bonds						11,360,000	11,360,000
Notes payable						95,000	95,000
Claims and judgments						194,490	194,490
Accrued compensated absences						1,375,125	1,375,125
Total liabilities	2,486,858	1,803,364		64,537		22,728,550	26,888,819
Fund equity:							
Investment in general fixed assets					\$15,473,223		15,473,223
Fund balances:							
Reserved for encumbrances	240,505						240,505
Reserved for debt service			\$1,404,625				1,404,625
Unreserved:							
Designated for specific fund purposes		851,359		4,456,834			5,308,193
Undesignated (Deficit)	(1,488,254)						(1,488,254)
Total fund equity	(1,247,749)	851,359	1,404,625	4,456,834	15,473,223		20,938,292
Total liabilities and fund equity	\$1,239,109	\$2,654,723	\$1,404,625	\$4,521,371	\$15,473,223	\$22,728,550	\$48,021,601

See accompanying notes to general purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS
COMBINED STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
ALL GOVERNMENTAL FUND TYPES
YEAR ENDED JUNE 30,2002**

	GOVERNMENTAL FUND TYPES				TOTALS (MEMORANDUM ONLY)
	General	Special Revenue	Debt Service	Capital Projects	
REVENUES					
Property taxes	\$2,196,134		\$562,551		\$2,758,685
Municipal license taxes	3,905,583				3,905,583
Licenses and permits	210,425				210,425
Intergovernmental	3,686,520	\$737,897		\$825,135	5,249,552
Rent of property	9,363				9,363
Fines and penalties	28,985				28,985
Interest	185,427				185,427
Federal grants		5,711,101			5,711,101
Miscellaneous	468,310	865		131	469,306
Total revenues	<u>10,690,747</u>	<u>6,449,863</u>	<u>562,551</u>	<u>825,266</u>	<u>18,528,427</u>
EXPENDITURES					
Current:					
Mayor and Municipal Assembly	770,792				770,792
General government	3,837,639	1,428,785			5,266,424
Public safety	786,568	241,074			1,027,642
Public works	3,251,838	7,560			3,259,398
Public health and sanitation	452,081				452,081
Welfare	235,069	3,623,125			3,858,194
Recreation	446,091	36			446,127
Human services	69,687				69,687
Principal retirement			2,246,595		2,246,595
Interest			489,023		489,023
Capital outlays	15,858	1,428,643		735,973	2,180,474
Total expenditures	<u>9,865,623</u>	<u>6,729,223</u>	<u>2,735,618</u>	<u>735,973</u>	<u>20,066,437</u>
Excess (deficiency) of revenues over (under) expenditures	825,124	(279,360)	(2,173,067)	89,293	(1,538,010)
OTHER FINANCING SOURCES (USES):					
Operating transfers in (out)	(3,028,618)	1,051,926	1,976,692		-
Proceeds from bonds and notes issuance	2,220,000			2,440,000	4,660,000
Total other financing sources (uses)	<u>(808,618)</u>	<u>1,051,926</u>	<u>1,976,692</u>	<u>2,440,000</u>	
Excess (deficiency) of revenues and other financing sources over (under) expenditures and other financing (uses)	16,506	772,566	(196,375)	2,529,293	3,121,990
Fund balances (deficit) beginning, as restated	<u>(1,264,255)</u>	<u>78,793</u>	<u>1,601,000</u>	<u>1,927,541</u>	<u>2,343,079</u>
Fund balances (deficit), ending	<u>(\$1,247,749)</u>	<u>\$851,359</u>	<u>\$1,404,625</u>	<u>\$4,456,834</u>	<u>\$5,465,069</u>

See accompanying notes to general purpose financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS
COMBINED STATEMENT OF REVENUES, EXPENDITURES, ENCUMBRANCES,
AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL AND DEBT SERVICE FUNDS
YEAR ENDED JUNE 30, 2002

	GENERAL FUND			DEBT SERVICE FUND		
	Budget	Actual	Variance Favorable (Unfavorable)	Budget	Actual	Variance Favorable (Unfavorable)
REVENUES						
Property taxes	\$2,108,884	\$2,108,884	\$ -	\$621,323	\$562,551	(\$58,772)
Municipal license taxes	3,262,944	3,905,583	642,639			
Licenses and permits	162,417	210,425	48,008			
Intergovernmental	3,734,464	3,686,520	(47,944)			
Rent of property	6,765	9,363	2,598			
Fines and penalties	29,075	28,985	(90)			
Interest	138,852	170,988	32,136			
Miscellaneous	1,326,709	1,429,686	102,977			
Total revenues	<u>10,770,110</u>	<u>11,550,434</u>	<u>780,324</u>	<u>621,323</u>	<u>562,551</u>	<u>(58,772)</u>
EXPENDITURES AND ENCUMBRANCES:						
Current:						
Mayor and Municipal Assembly	843,090	818,435	24,655			
General government	3,840,722	3,747,669	93,053			
Public safety	791,469	789,304	2,165			
Public works	3,132,928	3,081,496	51,432			
Public health and sanitation	452,081	452,081	-			
Welfare	246,170	245,478	692			
Recreation	462,428	454,702	7,726			
Human services	70,405	69,687	718			
Capital outlays	21,892	15,858	6,034			
Debt service:						
Principal retirement				571,000	531,000	40,000
Interest				307,323	389,981	(82,658)
Total expenditures and encumbrances	<u>9,861,185</u>	<u>9,674,710</u>	<u>186,475</u>	<u>878,323</u>	<u>920,981</u>	<u>(42,658)</u>
Excess (deficiency) of revenues over (under) expenditures and encumbrances	908,925	1,875,724	966,799	(257,000)	(358,430)	(101,430)
OTHER FINANCING SOURCES (USES):						
Operating transfers in (out)	(908,925)	(938,981)	30,056	257,000	287,055	(30,055)
Total other financing sources (uses)	<u>(908,925)</u>	<u>(938,981)</u>	<u>30,056</u>	<u>257,000</u>	<u>287,055</u>	<u>(30,055)</u>
Excess (deficiency) of revenues and other financing sources over (under) expenditures, encumbrances and other financing (uses)	<u>-</u>	<u>936,743</u>	<u>996,855</u>	<u>-</u>	<u>(71,375)</u>	<u>(131,485)</u>
ADJUSTMENTS TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES:						
Net change in encumbrances		(64,013)				
GAAP adjustments to revenues		(859,688)				
GAAP adjustments to expenditures		(126,899)				
Adjustment to transfer in (out)		(2,089,637)			1,689,637	
Proceeds from operational bond issuance		2,220,000				
Lease Agreement principal payment					(1,715,595)	
Lease Agreement interests payment					(99,042)	
Fund balances (deficit) beginning, as restated		<u>(1,264,255)</u>			<u>1,601,000</u>	
Fund balances (deficit), ending		<u><u>(\$1,247,749)</u></u>			<u><u>1,404,625</u></u>	

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2002

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The **Municipality of Peñuelas** (the Municipality) was established in 1793. The Municipality's governmental system consists of an executive and a legislative body. It is governed by a Mayor and twelve members Municipal Assembly who are elected every four years through the Puerto Rico general elections.

The Municipality provides the following services: public safety, public works, culture and recreation, health, urban development and welfare.

The Municipality's general-purpose financial statements are presented in accordance with generally accepted accounting principles (GAAP), as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. A summary of the Municipality's significant accounting policies follows:

A. Financial reporting entity:

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of *Statement No. 14* of the Governmental Accounting Standards Board. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary government appoints a voting majority of the entity's governing body and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is the nature and significance of the relationship between the entity and a primary government is such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. Based on the above criteria there are no potential component units, which should be included in the general-purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

B. Basis of presentation:

The Municipality records its transactions in the fund types and account groups described below:

Governmental fund types:

Governmental funds are those through which most governmental functions are financed. The acquisition, use and balances of the Municipality's expendable financial resources and the related current liabilities are accounted for through governmental funds. The measurement focus is upon determination of changes in financial position, rather than upon net income determination. The following are the Municipality's governmental fund types:

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

Special Revenue - is used to account for the proceeds of specific revenue sources that are legally restricted to be expended for specific purposes.

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

Capital Projects - is used to account for financial resources to be used for the acquisition or construction of major capital facilities.

Account groups:

The account groups are used to maintain accounting control and accountability of the Municipality's general fixed assets and long-term debt. The Municipality's account groups are:

General Fixed Assets - is used to account for all fixed assets of the Municipality.

General Long-term Debt - is used to account for all long-term debt obligations of the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

C. Basis of accounting:

All governmental funds are accounted for using the modified accrual basis of accounting. Revenues are recognized when they become measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Revenues collected in advance of the fiscal year to which they apply are recorded as deferred revenues and recognized as revenues in the corresponding year. Expenditures are recorded when the liability is incurred, except for (1) interest on general long-term debt obligations which is recorded when due, and (2) accruals for vacation, sick leave, claims and judgments which are recorded in the general long-term debt account group.

In applying the susceptible to accrual concept to intergovernmental revenues, the legal and contractual requirements of the numerous individual programs are used as guidance. There are essentially two types of such revenues. In one situation, funds must be expended on the specific purpose or project before any amount is reimbursed to the Municipality; therefore, revenues are recognized based upon the expenditures recorded. In the other situation, funds are virtually unrestricted as to purpose of expenditure and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are recognized as revenues at the time of receipt or earlier if they meet the criteria of availability.

Licenses, permits, rent of property, fines, penalties and other miscellaneous revenues (except investment earnings) are recorded as revenues when received because they are generally not measurable until actually received.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

D. Reservations of fund balance:

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

Encumbrances - Represent future expenditures under purchases orders, contracts and other commitments issued for goods and services not received at year-end. Where the appropriations lapse at year-end these will be honored during subsequent year. Encumbrances constitute the equivalent of expenditures for budgetary purposes and, accordingly, are reported with expenditures in all budgetary basis statements.

Debt Service - Represents net assets available to finance future debt service payments.

E. Budgetary data:

In establishing the budgetary data presented in the general purpose financial statements, the Municipality follows these procedures, which are in accordance with the Municipal Law:

- Prior to May 31, the Major submits to the Municipal Assembly a proposed budget for the fiscal year commencing the following July 1. The proposed budget includes estimated expenditures and the means of financing them.
- The budget document is available for public inspection prior to its approval by the Municipal Assembly.
- Prior to July 1, the annual budget is legally enacted through passage of the annual appropriation ordinance.
- Subsequent to the enactment of the annual appropriation ordinance, the Municipal Assembly has the authority to make necessary adjustments to the budget. Adjustments made during the year are reflected in the budget information included in the general-purpose financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

E. Budgetary data (continued):

The budget is prepared following the modified accrual basis of accounting, except for the encumbrances that are recorded as expenditures under the budgetary basis and as a reserve of funds balances under GAAP and for the interfund transactions that are not included in the budgetary basis.

The actual result of operations, presented in the Statement of Revenues, Expenditures, Encumbrances, and Changes in Fund Balances-Budget and Actual-General and Debt Service Funds, is in conformity with the budgetary accounting of the Municipality for a better comparison with the budget information.

The budget prepared for each of the special revenue funds is based on a program period, which is not necessarily the same as the Municipality's fiscal year. Accordingly, it is not practical to present an annual comparison of budget and actual for the special revenue funds.

F. Inventories:

The General Fund purchases office and printing supplies, gasoline, oil and other items. The cost of purchases is recorded as expenditure and, consequently, the inventory is not recorded in the general-purpose financial statements.

G. Property and equipment:

Property and equipment acquired are recorded as expenditures in the governmental funds and are capitalized at cost in the General Fixed Assets Account Group. Donated property and equipment are recorded at their estimated fair market value at the time they are received by the Municipality. No depreciation has been provided on property and equipment. Interest cost during the construction period is capitalized, when significant.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

H. Cash:

The Municipality's Director of Finance is responsible for investing available resources and is restricted by law to invest only in saving accounts and certificates of deposit with banks qualified as depositories of public funds by the Department of the Treasury of the Commonwealth of Puerto Rico. The Municipality maintains a cash pool that is available for use by all funds. Each fund type's portion of this pool is displayed on the combined balance sheet as Cash. All cash in banks at June 30, 2002 is insured by the Federal Deposit Insurance Corporation up to \$100,000, and by collateral held by the Treasury Department to its name. Interest earned from certificates of deposit and other short-term investments is recorded as revenue in the General Fund.

Cash with fiscal agent represents property tax collections retained by the Municipal Revenue Collection Center and Government Development Bank of the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, unused proceeds from bonds and notes issued for the acquisition or construction of permanent improvements and Federal grants resources.

I. Interfund transactions:

The Municipality has the following types of transactions among funds:

Operating transfers- Transfers that are reported when incurred as "Operating transfers from other fund" by the recipient fund and as "Operating transfers to other fund" by the disbursing fund.

Transfer of Expenditures (Reimbursements) - Reimbursement of expenditures made by one fund for another that are recorded as expenditures in the reimbursing fund and as reduction of expenditures in the reimbursed fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

J. Compensated absences:

Municipal employees are granted 30 days of vacation and 18 days of sick leave annually. Vacations may be accumulated up to a maximum of 60 days and sick leave up to a maximum of 90 days. In the event of an employee resignation, the employee is reimbursed for accumulated vacation days up to the maximum allowed. Separation from employment prior to the use of all or part of the sick leave before 10 years of service terminates all rights for compensation.

The Municipality accrues a liability for compensated absences, which meet the following criteria:

1. The Municipality's obligation relating to employee's rights to receive compensation for future absences is attributable to employee's services already rendered.
2. The obligation relates to rights that vest or accumulate.
3. Payment of the compensation is probable.
4. The amount can be reasonably estimated.

In accordance with the above criteria and requirements as established by *GASB Number 16*, the Municipality has accrued a liability for compensated absences, which has been earned but not taken by municipal employees. This liability is presented in the general long-term debt account group because they will not be funded with available expendable financial resources at June 30, 2002.

K. Insurance:

The Municipality has insurance coverage for its public facilities, primarily to provide protection from catastrophic losses. The Secretary of the Treasury Department of the Commonwealth of Puerto Rico is the agent commissioned to place all of the Municipality's insurance coverage.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

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

L. Total columns (memorandum only):

The total columns (memorandum only) are presented only to facilitate additional analysis. Consequently, amounts shown in total columns do not represent financial position or result of operations, in conformity with generally accepted accounting principles. Such data is not comparable to a consolidation since interfund eliminations have not been made.

M. Use of estimates in the preparation of general purpose financial statements:

The preparation of general purpose financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures at the date of the general purpose financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

N. Claims and judgments:

The estimated amount of the liability for claims and judgments, if any, which is due on demand, such as from adjudicated or settled claims, is recorded in the General Fund. The General Long-term Debt Account Group includes an amount estimated as a contingent liability or liabilities with a fixed or expected due date, which will require future available financial resources for its payment.

2. DUE TO OTHER GOVERNMENTAL ENTITIES:

The amounts due to other governmental entities in the General Fund include the following:

General Services Administration	\$ 6,526
Retirement System Administration	<u>2,687</u>
Total	<u><u>\$ 9,213</u></u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

2. DUE TO OTHER GOVERNMENTAL ENTITIES (CONTINUED):

The Municipality reached agreements with other governmental entities for the payment of debts on a long-term basis. These liabilities are presented in the General Long-Term Debt Account Group because they will not be funded with available expendable financial resources at June 30, 2002. The following is the balance of these accounts:

Municipal Revenue Collection Center (Property tax advances)	\$ 1,831,386
Department of Treasury (Property tax advances)	4,341,291
Department of Treasury (Social Security)	35,530
Department of Treasury (Case #93-1611)	27,000
Department of Treasury (Case #93-2579CCC)	90,830
Department of Treasury (Case #95-1030 CCC/ADC)	3,359,085
Department of Labor	18,813
Total	<u>\$ 9,703,935</u>

3. PROPERTY TAXES:

The Municipal Revenue Collection Center ("CRIM") of the Commonwealth of Puerto Rico is responsible by law to assess, levy and collect real and personal property taxes. The tax on personal property is self-assessed by the taxpayer. The assessment, as of January 1 of each year, is made on a return, which must be filed with the CRIM, together with the payment, by May 15 of each year. The tax on real property is assessed by the CRIM. The assessment is made as of January 1 of each year and is based on estimated current values of the property as of the year 1957.

Tax rates are 8.33% for real property and 6.33% for personal property of which 1.03% of both belongs to the Commonwealth of Puerto Rico. The Municipality's share is composed of the basic tax of 5.8% for real property and 3.8% for personal property, which is recorded in the General Fund, and the additional tax of 1.50% in both cases, which is restricted for debt service and retained by the CRIM for such purposes. To the extent that such taxes are informed and collected by the CRIM, they are recorded as revenue in the General Fund and in the Debt Service Fund.

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 CRIM assumes payment of the basic tax to the Municipality, except for property assessed at less than \$3,500, for which no payment is made. Revenue related to the basic tax on exempt property is recorded in the general fund when payments are received from the CRIM.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

3. PROPERTY TAXES (CONTINUED):

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

The CRIM advances to the municipality the estimated property tax collection for each fiscal year. Advances are repaid through actual collections from the taxpayers. The CRIM periodically informs the Municipality of the amounts collected and applied to outstanding advances. The property tax advanced by the CRIM during the year is recorded as property taxes revenues in the Municipality's General Fund. During the current year the actual collections were more than advances by \$287,419. Such amount was included as intergovernmental receivable in the General Fund. Also, the Municipality has a \$6,172,677 property tax advance debt balance from prior years (\$1,831,386 owed to CRIM, and \$4,341,291 owed to Treasury Department); such balance was included as a long-term debt in the General Long Term Debt Account Group because it will not be funded with available expendable financial resources at June 30, 2002.

4. MUNICIPAL LICENSE TAXES:

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

The tax rates are as follows:

Financial institutions	1.25%
Savings and loans associations	1.00%
Other organizations	0.40%

The tax may be paid in two equal semi-annual installments on July 15 and January 15 following the filing date. However, a discount of 5% is allowed for total payment received on or before April 15. Collections made prior to June 30 pertaining to the next fiscal year are recorded as deferred revenues.

5. INTERGOVERNMENTAL:

Intergovernmental revenues consist mainly of payments from the Commonwealth of Puerto Rico and payments in lieu of taxes from certain quasi-public corporations, principally the Puerto Rico Electric Power Authority.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

5. INTERGOVERNMENTAL (CONTINUED):

Grants and subsidies received from the Commonwealth of Puerto Rico include, among others, a general subsidy for capital improvements. Intergovernmental revenues are recorded in the General Fund, except for those related directly to capital improvements, which are recorded in the Capital Projects Fund.

6. DEBT SERVICE FUND:

Revenue for the Debt Service Fund consists mainly of the share of property taxes, which is designated for the debt service requirements of the bonds and notes obligations issued by the Municipality. The Government Development Bank pays principal and interest on these obligations.

7. GENERAL FIXED ASSETS:

A summary of changes in the General Fixed Assets Account Group is as follows:

Description	Balance July 1, 2001	Additions and adjustments	Retirements and adjustments	Balance June 30, 2002
Land	\$ 2,686,741	\$ -	\$ -	\$ 2,686,741
Building and Improvements	8,448,219			8,448,219
Machinery and Equipment	4,270,967	67,296		4,338,263
Total	\$ 15,405,927	\$ 67,296	\$ -	\$ 15,473,223

8. GENERAL OBLIGATION BONDS:

The general obligation bonds transactions for the year ended June 30, 2002 were as follows:

Balance at July 1, 2001	\$ 7,146,000
Debt issued	6,160,000
Principal retirements	(446,000)
Adjustments and/or Reclassifications	(1,500,000)
Balance at June 30, 2002	\$ 11,360,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

8. GENERAL OBLIGATION BONDS (CONTINUED):

General obligation bonds at June 30, 2002 are as follows:

Type of bonds	Maturity date	Original Amount	Range of Interest Rates	Balance at June 30, 2002
1980 Series	1-1-03	212,000	5.00%	\$ 15,000
1983 Series	1-1-05	182,000	5.00%	32,000
1985 Series	1-1-05	125,000	5.00%	28,000
1990 Series	7-1-04	315,000	3.26 to 8.40%	110,000
1994 Series	7-1-03	1,175,000	5.00 to 8.00%	310,000
1999 Series	7-1-18	2,630,000	5.00 to 7.81%	2,505,000
2001 Series	7-1-17	1,070,000	5.00 to 8.00%	1,045,000
2001 Series	7-1-10	1,300,000	5.00 to 8.00%	1,210,000
2002 Series	7-1-26	1,500,000	5.00 to 7.00%	1,480,000
2002 Series	7-1-26	135,000	5.00 to 7.00%	135,000
2002 Series	7-1-21	475,000	5.00 to 7.00%	475,000
2002 Series	7-1-26	1,965,000	5.00 to 7.00%	1,965,000
2002 Series	7-1-26	2,085,000	5.00 to 7.00%	2,050,000
Total general obligation bonds				<u>\$ 11,360,000</u>

The future annual requirements for the amortization of general obligations bonds outstanding as of June 30, 2002, are as follows:

Year ended June 30	Total
2003	\$ 519,000
2004	555,000
2005	431,000
2006	395,000
2007	415,000
Thereafter	<u>9,045,000</u>
Total	<u>\$ 11,360,000</u>

The Municipality is subject to certain laws of the Commonwealth of Puerto Rico, which limit the amount of bond debt to 10 percent of the assessed valuation of the property located in the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

9. NOTES AND LEASE OBLIGATIONS PAYABLE:

The notes payable transactions for the year ended June 30, 2002 were as follows:

Balance at July 1, 2001	\$ 180,000
Debt issued	-
Payments during the current year	(85,000)
	\$ 95,000
Balance at June 30, 2002	\$ 95,000

Notes payable at June 30, 2002 is as follows:

Description	Maturity Date	Original Amount	Range of Interest rates	Balance June 30, 2002
1998 Series	7-1-02	\$ 400,000	4.87% - 6.71%	\$ 95,000
Total notes payable				\$ 95,000

The future annual requirements for the amortization of notes payable outstanding as of June 30, 2002, are as follows:

Year ended June 30	Total
2003	\$ 95,000
Total	\$ 95,000

10. RETIREMENT PLAN:

Defined Benefit Pension Plan

The Employees' Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (the "System") is the administrator of a cost sharing multiple-employer defined benefit public employee retirement system established by the Commonwealth of Puerto Rico. The System was created under the Act 447 approved on May 15, 1951, as amended. All regular employees of the Municipality hired before January 1, 2000 and less than 55 years of age at the date of employment became members of the System as a condition to their employment. No benefits are payable if the participant receives a refund of his/her accumulated contributions. The System also provides for death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS -- (CONTINUED)

YEAR ENDED JUNE 30, 2002

10 RETIREMENT PLAN (CONTINUED):

Under the System, the employees and employer portions are contributed, for which, the employee amount is withheld from salaries. Covered employees are required by Commonwealth statute to contribute 5.775% for the first \$550 of monthly gross salaries plus 8.275% for the excess of this amount, or on the alternative, 8.275% of monthly gross salaries. The Municipality contributes to the System 9.275% of the participating employee's gross salaries.

Pension benefits for employees that joined the system before April 1, 1990 are as follows:

Years of Service	Participant Age	Pension Benefits
30 or more	54 or less	65% of the average of the three years of highest salary during the employees' service period.
30 or more	55 or more	75% of the average of the three of highest salary during the employees' service period.

For participants who retire with less than 30 years of service the pension benefits is computed at the rate of 1-1/2% of their average compensation for each year of credited service for the first 20 years and 2% for each of credited service for the remaining years.

For those employees that joined the system after April 1, 1980 the pension benefits are as follows:

Years of Service	Participant Age	Pension Benefits
25 or more	Between 55 and 64	Computed at the rate of 1-1/2% of their average compensation for each year of credited service, with an actuarial reduction based on the actuarial guides adopted by the Board of Trustees.
10 or more	65 or more	Computed at the rate of 1-1/2% of their average compensation for each year-credited service.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

10. RETIREMENT PLAN (CONTINUED):

For participants who retire with less than 25 years of service and the participant age are 64 or less the pension benefit is computed at the rate of 1-1/2% of their average compensation for each year of credited service.

Defined Contribution Plan

The Legislature of the Commonwealth enacted Act No. 305 on September 24, 1999, which amends Act No. 447 to establish, among other, a defined contribution saving plan program (the "Program") to be administered by the Retirement System. All regular employees hired for the first time on or after January 1, 2000 and former employees who participated in the defined benefit pension plan, received a refund of their contributions and are rehired on or after January 1, 2000 become members of the Program as a condition to their employment. In addition, employees who at December 14, 1999 were participants of the defined benefit pension plan, had the option, up to March 31, 2000, to irrevocably transfer their prior contributions to the defined benefit pension plan plus interest thereon to the Program.

Act No. 305 requires employees to contribute 8.275% of their monthly gross salary to the Program. Employees may elect to increase their contribution up to 10% of their monthly gross salary. Employee contributions are credited to his/her individual account established under the Program. Participants have three options to invest their contributions to the Program. Investment income is credited to the participant's account semi-annually.

The Municipality is required by the Act No. 305 to contribute 9.275% of the participant's gross salary. The System will use these contributions to increase its asset level and reduce the unfounded status of the defined benefits pension plan.

Upon retirement, the balance in the participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life and 50% of such benefit to the participant spouse in case of the participant death. Participants with balance of \$10,000 or less at retirement will receive a lump-sum payment. In case of death, the balance in the participant's account will be paid in a lump sum to his/her beneficiaries. Participants have the option of a lump sum or purchasing an annuity contract in case of permanent disability.

Total Municipality contributions to the above-mentioned plans during the year ended June 30, 2002 recorded as pension expenditures were approximately **\$261,000**. This amount represents 100% of the required contribution for the fiscal year ended June 30, 2002.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

10. RETIREMENT PLAN (CONTINUED):

The amount of the total pension benefit obligation is based on a standardized measurement established by GASB Number 27, *Accounting for Pensions by State and Local Governmental Employers*. The standardized measurement is the actuarial present value of credited projected benefits. This pension valuation method reflects the present value of estimated pension benefits that will be paid in future years as a result of employee's services performed to date and is adjusted for the effects of projected salary increases. The significant actuarial assumptions used to determine the standardized measure of the pension benefit obligation are summarized below:

- * The present value of the future pension payments was computed by using a discount rate of 8.5%. The discount rate is equal to the estimated long-term rate of return on current and future investments of the pension plan.
- * Future pension payments reflect an assumption of 5% salary increase.

The measure is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among other public retirement systems. The measure is independent of the actuarial funding method used to determine contributions to the plan.

The membership of retirees and beneficiaries currently receiving benefits and terminated employees entitled to benefits, but not yet receiving benefits, and active employees and the distribution of active employees between vested and nonvested is not readily available. Contributions in 2001 and prior years were made based on percentages established by the law. Such percentage has not been based on actuarial studies, as required by generally accepted accounting principles. An actuarial compilation of the annual contribution applicable to the Municipality has not been prepared. Accordingly, the accounts by which the actual contributions differ from the required actuarial contributions are not known.

The ten-year historical trend information is available in the separately issued audited financial statements of the Retirement System.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

11. INTERFUND TRANSACTIONS:

Due from/to other funds

Interfund receivables and payables represent temporary loans between the funds.

Operating transfers

Operating transfers represent transfers between funds to specific purposes designated by the management.

12. COMMITMENTS AND CONTINGENCIES:

A. Federal grants:

The Municipality participates in a number of Federal Financial Assistance Programs. These programs are subject to financial and compliance audits. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the Municipality expects such amounts, if any, not to be material.

B. Claims and lawsuits:

The Municipality is a defendant in legal matters that arise in the ordinary course of the Municipality's activities. With respect to pending and threatened litigation, the Municipality has reported liabilities of \$194,490 in the General Long Term Debt Account Group for anticipated unfavorable judgments. The amount presented in the general long term debt group of account represents the amount of estimated as probable liability, which will require future available financial resources for its payments. The administration believes that the ultimate liability, if any, would not be significant.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

13. BEGINNING FUND BALANCES (DEFICIT) RESTATEMENT:

The beginning Fund Balances (Deficit) for General and Debt Service Funds have been restated by situations detected during the fiscal year that affect the Fund Equity section of these Governmental Funds, as follows:

Description	General	Debt Service
Beginning Fund Balances (Deficit) at July 1, 2001	(\$ 1,101,004)	\$ 1,236,050
To adjust the fund balance due to the close of operations of a major business and the reimbursement of the Municipal License Tax to the taxpayer.	(256,261)	
To record an interfund transaction with a Federal Program	93,010	
To record prior years adjustments to CAE account made by the CRIM during the current year		364,950
Beginning Fund Balances (Deficit) at July 1, 2001, as restated	<u>(\$ 1,264,255)</u>	<u>\$ 1,601,000</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2002

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Expenditures
U.S. DEPARTMENT OF AGRICULTURE:			
Pass-through the Commonwealth of Puerto Rico - Department of Education:			
Child and Adult Care Food Program	10.558	Not Available	\$ 294,210
Total U.S. Department of Agriculture			294,210
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Section 8 Housing Choice Vouchers	14.871		732,535
Pass-through the Commonwealth of Puerto Rico - Office of the Commissioners of Municipal Affairs:			
Community Development Block Grant – State Program	14.228	99-FD-51 00-FD-51	1,238,360
Total U.S. Department of Housing and Urban Development			1,970,895
U.S. DEPARTMENT OF JUSTICE:			
Direct Program:			
Public Safety Partnerships and Community Policing Grant	16.710		192,121

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

<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>
Pass-through the Commonwealth of Puerto Rico - Department of Justice: Local Law Enforcement Block Grant	16.592	200-LB-VX-1085	8,385
Pass-through the Commonwealth of Puerto Rico- Department of Justice: Edward Byrne Memorial Grant	16.580	2000-DB-MMJP-01	<u>37,161</u>
Total U.S. Department of Justice			<u>237,667</u>

**U.S. FEDERAL EMERGENCY
MANAGEMENT AGENCY**

Pass-through the Commonwealth of Puerto Rico - Governor Authorized Representative (GAR): Public Assistance Grant	83.544	1247-DRPR	6,804
Hazard Mitigation Grant	83.548	1247-DRPR	116,363
Pass-through the Commonwealth of Puerto Rico - Emergency Management Agency: Emergency Management Performance Grant	83.552		<u>3,387</u>
Total U.S. Federal Emergency Management Agency			<u>126,554</u>

**U.S. DEPARTMENT OF HEALTH AND
HUMAN SERVICES**

Pass-through the Commonwealth of Puerto Rico - Administration for Children and Families:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

<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>
Child Care & Development Block Grant	93.575	Not Available	38,961
Pass-through the Commonwealth of Puerto Rico – Administration for Children and Families:			
Community Services Block Grant	93.569		35,142
Head Start Program	93.600	02-CH-483-22	<u>3,007,672</u>
Total U.S. Department of Health and Human Services			<u>3,081,775</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 5,711,101</u>

The accompanying notes are an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

1. BASIS OF PRESENTATION:

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

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue Fund in the Municipality's general-purpose financial statements. The reconciliation between the expenditures in the general-purpose financial statements and the expenditures in the Schedule of Expenditures of Federal Awards is as follows:

Description	Special Revenue
Per Schedule of Expenditures of Federal Awards	\$ 5,711,101
Non federal programs expenditures	<u>1,018,122</u>
Total expenditures in the general purpose financial Statements	<u>\$ 6,729,223</u>



López-Vega, CPA, PSC

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- Puerto Rico Society of Certified Public Accountants

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

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

We have audited the general purpose financial statements of the **Municipality of Peñuelas** as of and for the year ended June 30, 2002, and have issued our report thereon dated November 27, 2002, which was qualified because we been unable to audit the fixed assets of the general fixed assets account group. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the **Municipality of Peñuelas's** general purpose financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of general purpose 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 that are required to be reported under *Government Auditing Standards*.

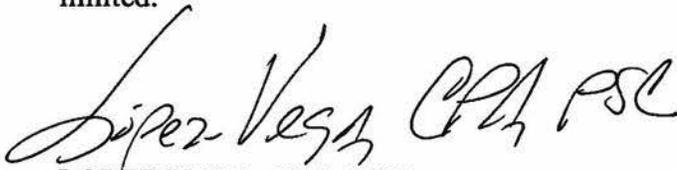
Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Peñuelas's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting that, in our judgment, could adversely affect **Municipality of Peñuelas's** ability to record, process, summarize, and report financial data consistent with the assertions of management in the general purpose financial statements. The reportable conditions are described in the accompanying schedule of findings and questioned costs items **02-01** through **02-04**.

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

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the general purpose financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose reportable conditions that are also considered to be material weaknesses. However, we believe item **02-01** of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management of the **Municipality of Peñuelas** in a separate letter dated November 27, 2002.

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
November 27, 2002

Stamp No. 1853990 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.





López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

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

**INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH OMB-CIRCULAR A-133**

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

Compliance

We have audited the compliance of the **Municipality of Peñuelas** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2002. The **Municipality of Peñuelas's** major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the **Municipality of Peñuelas's** management. Our responsibility is to express an opinion on the **Municipality of Peñuelas's** compliance based on our audit.

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

We were unable to obtain sufficient documentation supporting the compliance of the **Municipality of Peñuelas's** with the Head Start Program, regarding the earmarking requirements related to the administrative cost limits (finding 02-16), nor were we able to satisfy ourselves as to the **Municipality of Peñuelas's** compliance with those requirements by other auditing procedures.

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

In our opinion, except for the effects of such noncompliance, if any, as might have been determined had we been able to examine sufficient evidence regarding the **Municipality of Peñuelas's** compliance with the requirements of Head Start Program regarding the earmarking requirements related to the administrative cost limits, the **Municipality of Peñuelas's** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30,2002. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items, **02-05, 02-06, 02-08 and 02-10 through 02-15, 02-17 and 02-18.**

Internal Control Over Compliance

The management of the **Municipality of Peñuelas's** is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the **Municipality of Peñuelas's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the **Municipality of Peñuelas's** ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items **02-05 through 02-18.**

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees on the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weakness. However, of the reportable conditions described above we consider items **02-05, 02-06 and 02-10 through 02-15** to be material weaknesses.



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

We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the Municipality of **Peñuelas** in a separate letter dated February 18, 2003.

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.



LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
February 18, 2003

Stamp No. 1853991 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2002

Section I – Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued:	Qualified	
Internal control over financial reporting:		
Material weakness identified?	Yes X	No
Reportable conditions identified not considered to be material weaknesses?	Yes X	None reported
Noncompliance material to financial statements noted?	Yes	No X

Federal awards

Internal Control over major programs:		
Material weakness identified?	Yes X	No _____
Reportable conditions identified not considered to be material weaknesses?	Yes X	None reported
Type of auditors’ report issued on compliance for major programs:	Unqualified except for qualified for Head Start Program CFDA No 93.600	
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes X	No

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
14.871	Section 8 Housing Choice Voucher Program
93.600	Head Start Program

Dollar threshold used to distinguish between Type A and Type B programs	<u>\$ 300,000</u>	
Auditee qualified as low-risk auditee?	Yes	No X

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II – Financial Statements Findings

Finding Reference	02-01
Requirement	Fixed\ Capital Assets and Expenditures – Subsidiary Ledger
Statement of Condition	During our examination of the Municipality's property records and reports we noted the following deficiencies: balance in the Property Subsidiary Ledger does not reconcile with the ending balances reported in the audited financial statements; there is no adequate internal control procedures to assure the proper valuation and timeliness of recognition of real and personal property in the Property Subsidiary Ledger; and Construction in Progress account were not maintained in the General Ledger and Property Subsidiary Ledger.
Criteria	The federal regulations establish that a financial management system shall provide for effective control and accountability for all funds, property and other assets. Also, Article 9.002 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain updated property accounting records.
Cause of Condition	There is no internal control procedures implemented to assure the completeness of the property records and reports.
Effect of Condition	The Municipality did not maintain an adequate control of the accountability regarding equipment and real property transactions.
Recommendation	We recommend that the Municipality should implement procedures in order to assure the proper valuation and timeliness of recognition of real and personal property as well as Construction in Progress in the Property Subsidiary Ledger in a manner that it provides updated and complete financial information
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation will be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II - Financial Statements Findings

Finding Reference	02-02
Requirement	Accounting System
Statement of Condition	During our examination of the Municipality's accounting system we noted that it did not summarize the transactions in a formal General Ledger in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal Funds) and Account Groups.
Criteria	Article 8.010 of State Act Number 81 of August 30, 1991 states that Municipality should maintain an effective and updated accounting system.
Cause of Condition	The Municipality did not establish effective internal control over the transactions recorded on its accounting records. Also, the accounting data is not summarized in the form of a double-entry general ledger record.
Effect of Condition	The Municipality accounting records did not provide updated and complete financial information that presents the financial position and the result of operations and the change in fund balances. Such information is necessary to take management decisions.
Recommendation	We recommend that the Municipality should implement internal control and procedures in order to maintain an accounting system that contains information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, interfund transactions, etc.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation will be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II - Financial Statements Findings

Finding Reference **02-03**

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

Statement of Condition During our examination of the Municipality's procedures related to the purchasing and receiving process we examined sixty (60) disbursement vouchers and we noted the following situations:

- a. In thirteen (13) cases the requisitions weren't pre-numbered by responsible employer.
- b. In one (1) case the purchase order was issued after the receiving of services.
- c. In one (1) case the invoice wasn't signed.
- d. In two (2) cases the receiving report weren't signed by the employees that received of goods.
- e. In six (6) construction contracts weren't committed when executed. A purchase order was issued for each partial payment.
- f. In one (1) case the original certification submitted by the contractor was not available for our examination.
- g. Six (6) disbursement vouchers were not marked as paid.
- h. In two (2) cases the purchase order wasn't signed by the Finance Director and the voucher wasn't signed by Finance Director and by the employee who Pre-Audited.
- i. In two (2) cases the disbursement vouchers of asphalt, the invoices and receiving reports were not available on original.
- j. Three (3) quotations were not available for examination in five (5) disbursement vouchers.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II – Financial Statements Findings

Finding Reference	02-03 (Continued)
Criteria	The Revised Regulation on Basic Standards for the Municipalities of Puerto Rico establish in Chapter Four (4) that the Finance Director will be responsible to account and prepare disbursements through documents duly prepared and certified, including sufficient evidential matter to support the transactions. Also, Chapter Eight (8) of the Revised Regulation on Basic Standards for the Municipalities of Puerto Rico establishes the procedures related to the formal bids or quotations for the purchase of goods or services.
Cause of Condition	The Municipality did not establish effective internal control to assure that all transactions include all the required documentation.
Effect of Condition	The Municipality is not in compliance with the Revised Regulation on Basic Standards for the Municipalities of Puerto Rico.
Recommendation	We recommend that the Municipality should improve its internal control and procedures in order to assure that all disbursement vouchers contain all supporting documents before the payment is made. Also, we recommend that the Municipality should improve its procedures to assure that at least three (3) quotations would be requested for all purchase of goods or services that do not exceed \$10,000 and construction contracts that do not exceed \$40,000 or realize formal bids for purchases that exceed these limits. Also, authorization from Municipal Assembly should be requested before the acquisition of goods and services in which the bidder did not participated in the formal bid.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II – Financial Statements Findings

Finding Reference **02-04**

Requirement **Cash Receipts, Excise Taxes and Municipal License Taxes**

Statement of Condition We performed a cash receipt test and examined a sample of sixty (60) collections. The following will summarize the exceptions found:

- a. In six (6) cases the amount collected was deposited in the bank before the receipt was issued.
- b. In two (2) cases we didn't find a copy of the Income Tax Return in the Sales Volume Taxpayer's file.
- c. In three (3) cases we noted that the time extension to submit Municipal License Tax had expired and the Municipality did not receive the Audited Financial Statements.
- d. On twenty-one (21) occasions we found no supporting evidence for collections.
- e. We found no evidence of permits from "ARPE" needed to prepare the tax computation on two (2) taxpayers files for excise taxes
- f. The Municipality did not issue collection receipts for electronic fund transfers from U.S. Treasury Department related to Section 8 Housing Choice Voucher. The Program maintains a full set of accounting records apart from the Municipality's records.

Criteria

The Section Four (4) of the Chapter Three (3) of the Revised Regulation on Basic Standards for the Municipalities of Puerto Rico establishes that the Official Collector should realize a daily revision of amount collected and amounts credited in bank by governmental agencies to assure that the revenues have been duly processed in the period of collection.

The Chapter (9) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico states that the Municipality should maintain adequately documented taxpayer files including evidence of Audited Financial Statement in the case of taxpayers with a volume of business in excess of one million \$1,000,000, Municipal License Tax Certificate, etc.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II – Financial Statements Findings

Finding Reference 02-04 (Continued)

Article 6.005 (f) of State Act Number 81 of August 30, 1991 establishes that the Finance Director should maintain effective control and accountability over cash, real and personal property, and other assets.

Cause of Condition

The Municipality's internal control did not provide procedures to ensure that electronic fund transfers are recorded when received. Also, no adequate internal control procedures were implemented to ensure that taxpayer files are properly documented and daily collections and duly accounted. The Municipality did not establish effective internal control over the recording of revenues. Also, the Municipality did not establish effective internal control to assure that revenues were properly documented.

Effect of Condition

The Municipality did not maintain an adequate control to determine which taxpayer has submitted the required documentation to comply with excise tax and municipal license tax regulation. Also, the Municipality's accounting system did not provide updated and complete financial information that present the financial position and the result of operations and the change in fund balances. Such information is necessary to take management decisions.

Recommendation

Municipality should implement the following procedures in order to avoid these situations in a future:

- a. Maintain daily communication with the bank officials in order to assure that the cash receipts has been issued in the period that funds are transferred to the Municipality.
- b. Assign an employee to prepare a file including the "ARPE" estimate, contracts and other information necessary to assure that excise tax computation for construction projects are duly documented in order to be examined by the auditors.

COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section II - Financial Statements Findings

Finding Reference 02-04 (Continued)

- c. Assign an employee to review all Municipal License Tax taxpayers who requested a time extension in order to ascertain that they submitted the audited financial statement as required by law. In case of noncompliance with the time extension, the Municipality should proceed to eliminate the 5% discount taken and apply interest and penalties.
- d. We recommend that the Municipality's Official Treasurer should deposit cash collections daily. Also, we recommend that the Municipality Official Treasurer expedite the receipt before the funds are collected and deposited in the bank.

Questioned Costs None

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-05
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Cash Management
Statement of Condition	We realized Cash Management Test and after our procedures were performed we found that the Municipality requested funds that were not disbursed on a reasonable lapse of time and the programs maintained an excessive cash balance in books of approximately \$ 290,061. We noted that for seven months the leasing rate was under 95% and a revised requisition (Form 52663) was not submitted to HUD to reduce the monthly advances.
Criteria	Code of Federal Regulations 24, Subpart I, Section 85.20 (b) (7) requires a cash management system, and in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursement by the grantee.
Cause of Condition	The Municipality did not maintain effective control procedures over cash management.
Effect of Condition	The Municipality did not comply with the Code of Federal Regulations 24, Subpart I, Section 85.20 (b) (7).
Recommendation	We recommend to the Municipality's Management to periodically compare actual program cash requirements to the funds advanced from U. S. Treasury Department and prepare and submit a revised requisition to reduce monthly advances.
Questioned Costs	None
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-06
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Eligibility Test
Statement of Condition	<p>We performed an eligibility test and examined a sample of fifty nine (59) participant files. The following will summarize the exceptions found:</p> <ul style="list-style-type: none">a. In seven (7) cases there was no evidence of Application Form in the participant file.b. In twenty-nine (29) cases there was no signature on one or more Release Forms to allow the PHA to obtain information from third parties.c. In twenty-nine (29) participant files the Release Form to allow the PHA to obtain information from third parties did not contain the minimum information required.d. In fifty-nine (59) cases there was no Privacy Act Notice form signed by the head of household.e. In twenty (20) cases some members of the family who are at least 18 years old did not sign the application form and/or other release forms included in the participant's file.f. In fifteen (15) cases the files revealed deficiencies in terms of lack of official income sources such as alimony or disability, actual photos (family composition), copy of social security check or certification and social security card.g. In one (1) case the release form to allow the PHA to obtain information from third parties and the release for employment information were not complete for annual reexamination. These forms were completed when a change of unit was done, prior to the reexamination was made.

COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 02-06 (Continued)

- h. In one (1) case the necessary information and documentation to verify income eligibility was required after contract execution.
- i. In one (1) case the PHA accepted a new tenant without having all documents of eligibility such as: evidence of income, notarized statement and family composition.
- j. We noted that in five (5) participant files the PHA determined the Housing Assistance Payment for the fiscal year 2001-2002 using incomplete supporting evidence of family annual income.
- k. In thirty-two (32) cases the Municipality did not show consistency in the payment standard used to calculate the Housing Assistance Payments.

Criteria

Code of Federal Regulations 24, Sections 5.212, 5.230, and 5.601 through 5.617 as a condition of admission or continued occupancy, it require the tenant and other family members to provide necessary information, documentation and releases for the PHA to verify income eligibility. The PHA has to reexamine family income and composition at least once every twelve months and adjust the tenant rent and housing assistance payment as necessary. As part of this regulation the participant and other members of the family who are at least 18 years old must sign an application form, one or more releases forms, a Federal-Prescribed General Release Form for employment information and a Privacy Act Notice. Also, requires the PHA to reexamine family income and composition at least once every twelve months and adjust the tenant rent and housing assistance payment as necessary

Code of Federal Regulations 24, Sections 982.201, 982.515 and 982.516 establish income eligibility and tenant's rent payment calculation requirements. The Housing Choice Voucher Guidebook, Chapter six (6) establishes procedures for the HAP payments calculation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-06 (Continued)
Cause of Condition	The Municipality did not have adequate internal control procedures to assure that the participant's files include all required documentation and releases required by federal agencies. The Federal Program Department did not perform adequate monitoring procedures to assure that all HAP payments are duly computed by the program staff
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Sections 5.212, 5.230, 5.601 through 5.617, 982.201 and 982.515.
Recommendation	We recommend the Program to establish the following procedures: <ol style="list-style-type: none">a. Provide an application form to be filled by the participant and sign by all members of the family who are at least 18 years old.b. Provide a Federal-Prescribed General Release Form for employment information and a privacy act notice to be signed by all members of the family who are at least 18 years old.c. Implement internal control procedures to assure that the participant's files include all documentation required by federal agencies.d. We recommend management to establish to monitoring procedures to assure that HAPs are duly computed as required by the Federal Regulations.
Questioned Costs	None
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-07
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Reporting - Financial Reporting
Statement of Condition	During our examination of Reporting test, we noted that the program accountant prepared the accounting information after year-end. The accounting records were completed to prepare the HUD-52681 Vouchers for Payment of Annual Contributions and Operating Statement (OMB No. 2577-0149) for the year ended June 30, 2002.
Criteria	Code of Federal Regulations 24, Section 85.20 (b) (2) states that the grantee must maintain records, which adequately identify the source and application of funds, provided for financially assisted activities.
Cause of Condition	The program does not maintain adequate controls to assure that all transactions are posted at end of the month, thus, at the end of year the general ledger is completed.
Effect of Condition	The program did not maintain complete and accurate accounts and other records for the program in accordance with HUD requirements.
Recommendation	We recommended to management to implement internal control procedures to maintain adequate and accurate accounting records throughout the entire fiscal year.
Questioned Costs	None
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-08
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Performance Reporting
Statement of Condition	We noted that the program answer a (yes) in the items 2 (a) (b), 4, 5 and item 6 and we noted that the program did not comply with those requirements as per our test results.
Criteria.	Code of Federal Regulations 24, Section 985.3 stated that HUD 52648, SEMAP certification and the Addendum for Reporting Data for Deconcentration Bonus Indicator for PHAs with jurisdictions in metropolitan FMR areas should be submitted to HUD who will realize on site visits and verify the independent auditors annual audit reports to assure the compliance with this requirement.
Cause of Condition	The program does not maintain adequate controls to provide sufficient evidence to support the compliance with the answers detailed in the SEMAP Report submitted to HUD.
Effect of Condition	The Municipality is in not compliance with Code of Federal Regulations 24, Section 985.3.
Recommendation	We recommend to the Municipality to establish adequate internal control procedures to assure that the program complies with federal regulations and maintain proper records to support SEMAP Report answers.
Questioned Costs	None
Management Response	The Municipality has establishes procedures to assure the compliance with this requirement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-09
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Reporting – Special Reporting
Statement of Condition	<p>During our verification of fifty-nine (59) participant files we noted the following deficiencies:</p> <ul style="list-style-type: none">a. We noted that on thirty-two (32) participant files the HUD 50058 Form, Family Report (OMB No. 2577-0083), were not printed and maintained in the participant files every time there was a change in family composition, family income or other situations that may affect the calculation of the total tenant payment. Only a HUD 50058 Form was manually completed and maintained on each file.b. In twenty-five (25) cases the HUD 50058 Form, Family Report (OMB No. 2577-0083), revealed deficiencies in terms of data entry such as: names, last unit passed, unit address, social security number and date of birth reported.
Criteria	<p>Code of Federal Regulation 24, Sec.908, establishes that PHA must submit HUD-50058 Form, Family Report (OMB No. 2577-0083), electronically to HUD each time the PHA completes an admission, annual reexamination, interim reexamination, portability move-in, other change of unit for a family, etc.</p>
Cause of Condition	<p>The HUD 50058 Form, Family Report (OMB No. 2577-0083) was not printed and maintained in the participant file every time there was a change in family composition, family income or other situations that may affect the calculation of the total tenant payment.</p>
Effect of Condition	<p>The Municipality did not maintain evidence regarding compliance with the Code of Federal Regulation 24, Sec. 908.</p>

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-09 (Continued)**

Recommendation Municipality should implement the following procedures in order to avoid these situations in the future:

- a. We recommend that the HUD 50058 Form, Family Report (OMB No. 2577-0083), be printed and maintained in the participant file every time there is a change in family composition, family income or other situations that may affect the calculation of the total tenant payment.
- b. Assign an employee to review the HUD 50058 Form, Family Report (OMB No. 2577-0083), to assure that the information submitted electronically to HUD did not contain errors in order to be evaluated correctly by HUD personal.

Questioned Costs None

Management Response The Federal Programs Office will implement controls to assure that applicable documentation of the determination of reasonable rent is maintained in participant's files.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-10
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 Municipality did not maintain an up-to-date utility allowance schedule for the audit period ending June 30, 2002. There is no evidence of the last time that the Utility Allowance Schedule was actualized.
Criteria	Code of Federal Regulations 24, Section 982.517 states that the Municipality must maintain an up-to-date utility allowance schedule. The Municipality must review the utility rate data for each utility category each year 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 Municipality did not follow the procedures established to review utility rate data each year.
Effect of Condition	The Municipality is no in compliance with Code of Federal Regulations, 24, Section 982.517.
Recommendation	The Municipality should evaluate utility allowance rate each year as established in the federal regulations.
Questioned Costs	None.
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-11
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
Statement of Condition	During our verification of fifty-nine (59) participant files we noted the following exceptions: <ul style="list-style-type: none">a. In fifty-seven (57) participant files there no evidence of quality control re-inspections performed and documented by a reasonable official.b. In five (5) cases were the correction period had ended no evidence was found to support that corrections required by PHA were completed. Also, no evidence was found in each file that showed the PHA properly stopped (abated) HAP's or terminated the HAP contract.
Criteria	Code of Federal Regulations 24, Subpart I, 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	Management does not have adequate internal control procedures to assure that annual inspections and quality control re-inspections are realized and properly documented.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Section 982.158 (d) and 982.405 (b)
Recommendation	We recommend management to implement internal control procedures to assure that annual inspections and quality control re-inspections are realized and properly documented.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-11 (Continued)**

Questioned Costs **None**

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-12
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Selection from the Section 8 Waiting List
Statement of Condition	During our verification of eligibility and waiting list tests, we noted the following exceptions: <ul style="list-style-type: none">a. The Municipality accepted a participant that was not included in the waiting list. The participant file did not show that it was selected by emergency or other reason contemplated in the Administrative Plan.b. The Municipality did not selected a family who was top of the waiting list because the unit size available was greater that the family composition. The Municipality selected to the next family in waiting list with a family composition similar at the available unit.
Criteria	Code of Federal Regulations 24, Subpart E, Section 982.203 (a) (2) states that the PHA may admit a family that is not on the PHA waiting list or without considering the family’s waiting list position. The PHA must maintain records showing that the family was admitted with HUD-targeted assistance. Code of Federal Regulations 24, CFR, Subpart E, Section 982.204 (d) states that the Family Size (1) the order of admission from the waiting list may not be based on family size or on the family unit size for which the family qualifies under the PHA occupancy policy.
Cause of Condition	The Federal Program did not perform adequate monitoring procedures to assure the existence and maintenance of a waiting list and to assure that participants were selected from the top of the waiting list.
Effect of Condition	Municipality is not in compliance with 24 CFR, Subpart E, Section 982.203 (a) (2) and 982.204 (d).

COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-12 (Continued)**

Recommendation We recommended management to explain in the file the reason of selection of a participant which was not included in the waiting list. The Management should comply with all requirements of the regulation program and administrative plan. Also, we recommended management to have caution and do not skip the applications by reasons not included in the administrative plan.

Questioned Costs None

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-13
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test – Reasonable Rent
Statement of Condition	During our verification of fifty-nine (59) participant files we noted that on fifty-seven (57) participant files the determination of reasonable rent was not documented in the participant file.
Criteria	Code of Federal Regulations 24, Sections 982.54 (d)(15), 982.158 (f)(7) and 982.507 states that the PHA must determine reasonable rent at the time of the initial leasing and must maintain records to document the basis for the determination that the rent paid to the owner is reasonable.
Cause of Condition	The Municipality did not maintain records to document the basis for the determination that the rent paid to the owner was reasonable.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Sections 982.54 (d)(15), 982.158 (f)(7) and 982.507.
Recommendation	We recommend that the Municipality should implement controls to assure appropriate documentation of the determination of reasonable rent is maintained in participants file.
Questioned Costs	None
Management Response	The Municipal Office of Federal Programs will implement controls to assure that applicable documentation of the determination of reasonable rent is maintained in participant's files.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-14
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State - Commonwealth of Puerto Rico Administration for Children and Families (ADFAN)
Requirement	Cash Management
Statement of Condition	During our Cash Management test we found that the Municipality requested funds that were not disbursed on a reasonable lapse of time. The program maintained an excessive average cash balance in books of \$ 134,226
Criteria	Code of Federal Regulations 45, Subpart C, Section 92.20 (b) (7) states that the Municipality must maintain procedures for minimizing the time elapsed between the transfer of funds from the U.S. Treasury and disbursement is made by the Municipality.
Cause of Condition	The Municipality did not maintain appropriate cash management procedures in order to request funds to the Administration for Children and Families only for immediate needs.
Effect of Condition	The Municipality requested funds in excess of immediate needs, thus, is not in compliance with Code of Federal Regulations 45, Subpart C, Section 92.20 (b) (7).
Recommendation	We recommend management to continue strengthen its procedures to minimize the time elapsed between the transfer of funds from the Administration for Children and Families and the disbursements made by the Municipality.
Questioned Costs	None
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-15
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through Sate - Commonwealth of Puerto Rico Administration for Children and Families (ADFAN)
Requirement	Davis-Bacon Act
Statement of Condition	During our Davis-Bacon Act test, we noted that the Municipality did not apply adequately the monitoring system developed to ensure contractors compliance with payment of prevailing wages rates to employees. The contractors were not informed in the procurement process of the requirement of the Davis Bacon Act, thus, they were not required to submit certification and copies of payrolls (weekly payrolls) including the prevailing wage rates. We noted that in the file of Davis Bacon Act the Municipality did not maintain the prevailing wages rates notice.
Criteria	Davis-Bacon Act, as amended (40 USC 276-276A-5), Subpart K, 24 CFR 570.503.
Cause of Condition	The Municipality did not apply all monitoring system developed by it to test applicable contractors with respect to payment of prevailing wages.
Effect of Condition	The Municipality is not in compliance with Davis-Bacon Act as amended (40 USC 276A-276A-5)
Recommendation	We recommend management to follow monitoring system procedures developed, including obtaining contractor's and subcontractor's weekly payrolls to be reviewed weekly by responsible Municipal Employee. Also, interview contractor's and subcontractor's laborers periodically (up to ten percent (10%) of the workers on long term projects) in order to establish the degree of compliance and the nature and extend of violations, if any.
Questioned Costs	None
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-16
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State - Commonwealth of Puerto Rico Administration for Children and Families (ADFAN)
Requirement	Matching, Level of Effort, Earmarking - Administrative Cost Limits
Statement of Condition	The Accounting System maintained for Head Start Program financial activities did not provide for the classification of financial transactions between administration and programmatic costs. Alternate procedures were used by the program staff to compute compliance with the fifteen percentage (15%) administrative cost limit. We were unable to determine if the Municipality complies with this requirement.
Criteria	Code of Federal Regulations 45, Subpart C, Section 92.20 9 (a) (2) states that the grantees must maintain fiscal controls and accounting procedures sufficient to permit the tracing of funds to a level of expenditures, necessary to establish that such funds have not been used in violation of the restriction and prohibitions of applicable statutes.
Cause of Condition	The Municipality did not maintain adequate internal controls to assure the accountability of all transactions in accordance with Federal regulations
Effect of Condition	Such condition may cause Municipality Management non-compliance with certain compliance requirements like allowable costs, activities allowed and unallowable and earmarking.
Recommendation	We recommend to the Municipality's Management to modify the Computerized Accounting System chart of accounts to create separate accounts for administrative and programmatic expenditures. Also, cost with dual benefits (administrative and programmatic) should be identified and allocated appropriately using a cost-benefit proportion.
Questioned Costs	None
Management Response	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-17
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State - Commonwealth of Puerto Rico Administration for Children and Families (ADFAN)
Requirement	Matching, Level of Effort, Earmarking - Enrollment Level
Statement of Condition	<p>During our enrollment level test we examined forty (40) participant files and noted the following exceptions:</p> <ul style="list-style-type: none">a. Six (6) participant files had incomplete supporting evidence of family annual income.b. In one (1) case the participants came from families whose income exceeded applicable poverty guidelines.
Criteria	<p>Code of Federal Regulations 45, Section 1305.4 (b) (1) states that at least ninety percentages (90%) of participants who are enrolled in each Head Start program must be from low-income families. Code of Federal Regulations 45, Section 1305.4 (c) (d) (e) states that family income must be verified by program staff before determining that an applicant is eligible. The program staff must verify income tax returns, W-2 forms, pay stubs and other; and must sign a statement identifying which of income supporting documents were examined. Also, the program staff must state that the participant is eligible to participate to participate in the Program.</p>
Cause of Condition	<p>The Municipality did not maintain adequate internal controls to assure compliance with Program regulations.</p>
Effect of Condition	<p>Such condition may cause Municipality's non-compliance with earmarking - enrollment level requirements.</p>
Recommendation	<p>We recommend to the Municipality Management to maintain a formal participants selection process which ensure compliance with the Head Start program requirements.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-17 (Continued)**

Questioned Costs **None**

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	02-18
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State - Commonwealth of Puerto Rico Administration for Children and Families (ADFAN)
Requirement	Special Test-Licensing Requirement
Statement of Condition	<p>In our Special Test-Licenses Verification for thirteen (13) centers used by Head Start we noted the following exceptions:</p> <ul style="list-style-type: none">a) In one (1) case the Fire Department license was expired.b) In one (1) case the Health Department license was not available for our examination.c) The Administration for Children and Families license was expired in seven (7) centers.
Criteria	<p>Code of Federal Regulations 45, Subpart C, Section 1306.30 (c), states that the facilities used by Head Start grantees for regularly scheduled center-based and combination program option class room activities or home-based group socialization activities must comply with applicable State and Local requirements concerning licensing.</p>
Cause of Condition	<p>The Municipality did not establish procedures to assure that Head Start centers maintain actualized licenses from the Administration for Children and Families.</p>
Effect of Condition	<p>The Municipality is not in compliance with 45 CFR, Section 1306.30 (c).</p>
Recommendation	<p>The Municipality should establish routine visits to the different centers in order to assure that the centers are in conditions necessary to comply with the licensing requirement. We also recommend that the Municipality should review Centers files to assure completeness of the required documentation and perform periodically follow-up procedures in order to update such files.</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS - (CONTINUED)

YEAR ENDED JUNE 30, 2002

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference **02-18 (Continued)**

Questioned Costs None

Management Response The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PEÑUELAS**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS

YEAR ENDED JUNE 30, 2002

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
01-05	14.855 14.857	<u>The disbursement vouchers paid by the program and the supporting documents for that payments were not stamped as paid.</u> Full corrective action has been taken.
01-06	14.855 14.857	<u>Eligibility Test</u> No corrective action has been taken.
01-07	14.855 14.857	<u>Reporting - Financial Reporting</u> No corrective action has been taken.
01-08	14.855 14.857	<u>The SEMAP report was not available for our examination.</u> No corrective action has been taken.
01-09	14.855 14.857	<u>Reporting - Special Reporting</u> No corrective action has been taken.
01-10	14.855 14.857	<u>Special Test - Housing Quality Standards Inspections</u> No corrective action has been taken.
01-11	14.855 14.857	<u>The waiting list maintained by the Municipality did not contain all required information</u> Partial corrective action has been taken.
01-12	14.855 14.857	<u>Special Test - Reasonable Rent</u>

**COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS – (CONTINUED)

YEAR ENDED JUNE 30, 2002

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		No corrective action has been taken.
00-III-02	14.228 14.855 14.857	<u>Allowable Cost\Cost Principles</u> Full corrective action has been taken for Section 8 program. No corrective action plan for SBGP program.
00-III-03	14.855 14.857	<u>Allowable Cost\Cost Principles</u> Full corrective action has been taken.
00-III-07	14.855 14.857	<u>Reporting</u> No corrective action has been taken.
00-III-08	14.855 14.857	<u>Special Tests and Provisions</u> No corrective action has been taken.
00-III-09	14.855 14.857	<u>Special Tests and Provisions</u> No corrective action has been taken.