

**OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES  
ÁREA DE ASESORAMIENTO, REGLAMENTACIÓN E INTERVENCIÓN FISCAL  
ÁREA DE ARCHIVO DIGITAL**

**MUNICIPIO DE PEÑUELAS  
AUDITORÍA 2007-2008  
30 DE JUNIO DE 2008**

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**BASIC FINANCIAL STATEMENTS ACCOMPANIED BY  
REQUIRED SUPPLEMENTARY INFORMATION  
SINGLE AUDIT  
YEAR ENDED JUNE 30, 2008**

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COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

BASIC FINANCIAL STATEMENTS ACCOMPANIED BY  
REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2008

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COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2008

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

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Peñuelas, Puerto Rico, as of and for the year ended June 30, 2008, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these 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 and the applicable to financial audit contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Note 12, the Municipality has not maintained complete and adequate records in order to obtain sufficient and competent evidential matter related to the Capital Assets reported in the governmental activities and, accordingly, the amount by which this departure would affect the assets, net assets, and expenses of the governmental activities is not reasonably determinable.

In our opinion, because of the effects of the matter discussed in the third paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the governmental activities of the Municipality of Peñuelas, Puerto Rico, as of June 30, 2008, and the changes in financial position, thereof for the year then ended.

INDEPENDENT AUDITORS' REPORT

Municipality of Peñuelas

Page 2

In addition, in our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of each major fund, and the aggregate remaining fund information of the Municipality of Peñuelas, Puerto Rico, as of June 30, 2008, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 3 through 10 and the Budgetary Comparison Schedule-General Fund on page 40 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated February 24, 2009, on our consideration of the Municipality's internal control structure over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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 basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

The accompanying Financial Data Schedule is presented for purposes of additional analysis required by U.S. Department of Housing and Urban Development and is not required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Mendoza & Ramos CPA's  
Mendoza & Ramos, C.S.P.  
Certified Public Accountant

Guayama, Puerto Rico  
December 11, 2008, except for Financial Data Schedule which is dated on March 27, 2009.

The stamp number 2395334  
was affixed to the original  
of this report.



**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED JUNE 30, 2008**

This discussion and analysis of the Municipality of Peñuelas (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2008. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2003, first year of implementation of Governmental Accounting Standards Board (GASB) Statement No. 34, "Basic Financial Statements - and Management's Discussion and Analysis-for State and Local Governments." This MD & A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following mayor information:

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

**FINANCIAL HIGHLIGHTS**

The following comments about the financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2008 deserve special mention:

1. Total assets of the Municipality amounted to \$45,099,259 (\$41,351,833 in 2007) which represents an increase of 9.1% (21.1% in 2007) compared to prior fiscal year.
2. At the end of fiscal year 2008, total liabilities amounted to \$34,717,593 (\$31,986,696 in 2007). Out of said amount, \$28,146,941 (\$24,984,211 in 2007) corresponded to long-term liabilities of which \$24,121,000 (\$21,151,000 in 2007) represented the outstanding balance of bonds issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.
3. Total net assets of the Municipality amounted to \$10,381,666 (\$9,365,137 in 2007) which represents an increase of 10.9% (336.2% in 2007) compared to prior fiscal year.
4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$24,648,848 (\$27,725,440 in prior fiscal year) derived from the following sources: \$225,817 (\$47,873 in prior fiscal year) charges for services; \$6,596,312 (\$9,807,340 in prior fiscal year) from operating grants and contributions; \$1,039,379 (\$1,910,070 in prior fiscal year) from capital grants and contributions

obtained from other sources, and \$16,787,340 (\$15,960,157 in prior fiscal year) from general revenues available.

## **FINANCIAL HIGHLIGHTS (CONTINUED)**

5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$23,582,649 (\$20,542,485 during fiscal year 2007).
6. As reflected in the Statement of Activities, the current fiscal year operations contributed to an increase in the Net Assets figure by \$1,066,199 (\$7,337,550 during fiscal year 2007).
7. As of the close of the current fiscal, the Municipality's Governmental Funds reported combined ending fund balances of \$17,412,813 (\$15,817,741 as of June 30, 2007).
8. As the end of the current fiscal year the Municipality's General Fund balance amounted to \$1,546,060, compared to a fund balance of \$1,066,233 in the prior fiscal year, as restated.
9. The actual General Fund budgetary activities resulted in a favorable balance of \$491,685 (\$2,713,409 during the prior fiscal year), caused mainly due to savings in general government and public works expenditures.

## **FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION**

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2008. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

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

## **FINANCIAL STATEMENTS COMPONENTS**

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

The Statement of Net Assets reflects information of the Municipality as a whole of a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year. Such financial level is measured as the difference between total

## FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

assets and liabilities, with the difference between both items reported as net assets. It is important to note that although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations. The higher the increments achieved in net revenues, the higher the capacity to increase the net assets figure either thru additional borrowings or thru internally generated funds. This in turn will benefit the welfare of Peñuelas constituents.

The Statement of Activities is focused on both gross and net cost of the various activities of the Municipality. It presents information which shows the changes in the Municipality's net assets at the most recent fiscal year. Based on the use of the accrual basis of accounting, changes are reported as soon as the underlying event occurs, regardless of the timing of the related cash flows. Under said approach, revenues and expenses are reported in the Statement of Activities based on the theory that it will result in cash flows to be realized in future periods.

A brief review of The Statements of Activities of the Municipality at June 30, 2008, shows total expenses incurred to afford the cost of all functions and programs amounted to \$23,582,649 (\$20,387,840 during prior year). Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$7,861,508 (\$11,765,283 during prior year) was derived from the following sources: \$225,817 (\$47,873 in prior fiscal year) charges for services; \$6,596,312 (\$9,807,340 in prior fiscal year) from operating grants and contributions; and \$1,039,379 (\$1,910,070 in prior fiscal year) from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$16,787,340 (\$15,960,157 in prior fiscal year). When such figure is added to the \$7,861,508 (\$11,765,283 during prior year) previously mentioned, total revenues available for the financing of activities amounted to \$24,648,848 (\$27,725,440 during prior year). There was an excess of revenues over expenses in the amount of \$1,066,199 (\$7,337,550 during prior year) which contributed with an increase to the figure of net assets attained at the end of the fiscal year.

The Fund Financial Statement is another important component of the Municipality's financial statements. A fund is a grouping of related accounts that are used to maintain accountability and controls over economic resources of the Municipality that have been segregated for specific activities. The Municipal fund type of accounting is used to demonstrate compliance with related legal requirements. Information offered thru this Statement is limited to the Municipality most significant funds and is particularly related to the local government only, instead of the government as a whole. Government funds are used to account for essentially the same functions as those reported as governmental activities. The funds are reported using an accounting method known as modified accrual accounting which measures cash and all other financial assets that can be readily converted into cash.

The fund statement approach gives the user a short term view of the Municipality's government operations and the basic services it provides. Since the focus of government funds is narrower than that of the financial statements as a whole, it also helps the user with comparable information presented in the governmental activities report. By doing so, readers of the basic financial statements may understand better the long-term effect of the Municipality's short-term financial decisions.

## INFRASTRUCTURE ASSETS

Historically, a significant group of infrastructure assets such as roads, bridges, traffic signals, underground pipes not associated with utilities, have not been recognized nor depreciated in the accounting records of the Municipality. GASB 34 requires that such type of assets be inventoried, valued and reported under the governmental column of the Government-Wide Statement. As of July 1, 2002, the Municipality commenced the prospective reporting of infrastructure assets. The Municipality reports historical costs of infrastructure assets during the fiscal year beginning on July 1, 2006.

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

## FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

### Net Assets

The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Peñuelas, primary government liabilities exceeded total assets by \$10,381,666 at the end of 2008, compared to \$9,365,137 at the end of the previous year, as showed in the following condensed Statement of Net Assets of the Primary Government.

Condensed Statement of Net Assets	2008	2007	Change	%
<b>Assets</b>				
Current assets	\$ 23,249,578	\$ 22,095,282	\$ 1,154,296	5.2%
Capital assets	21,849,681	19,256,551	2,593,130	13.5%
<b>Total assets</b>	<b>45,099,259</b>	<b>41,351,833</b>	<b>3,747,426</b>	<b>9.1%</b>
<b>Liabilities</b>				
Current liabilities	8,003,188	8,180,101	(176,913)	-2.2%
Noncurrent liabilities:	26,714,405	23,806,595	2,907,810	12.2%
<b>Total liabilities</b>	<b>34,717,593</b>	<b>31,986,696</b>	<b>2,730,897</b>	<b>8.5%</b>
<b>Net Assets</b>				
Invested in capital assets, net of related debt	3,844,682	4,311,551	(466,869)	-10.8%
Restricted	15,124,950	14,070,074	1,054,876	7.5%
Unrestricted (deficit)	(8,587,966)	(9,016,488)	428,522	-4.8%
<b>Total net assets</b>	<b>\$ 10,381,666</b>	<b>\$ 9,365,137</b>	<b>\$ 1,016,529</b>	<b>10.9%</b>

## Changes in Net Assets

The Statement of Activities reflects that for fiscal year 2008, the net effect of revenues derived from several programs plus current operating revenues compared to the total expenses, amounted to \$1,066,199 (\$7,337,550 during prior year) increase in the Municipality's net assets. Approximately 52 (43 in prior fiscal year) percent of the Municipality's total revenue came from taxes, while 44 (53 in prior fiscal year) percent resulted from grants and contributions, including federal aid. Charges for Services and other miscellaneous revenues provided 4 (4 in prior fiscal year) percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for general government, health and welfare services and public works. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

Condensed Statement of Activities	2008	2007	Change	%
<b>REVENUES</b>				
Program Revenues:				
Charges for Services	\$ 225,817	\$ 47,873	\$ 177,944	371.7%
Operating Grants and Contributions	6,596,312	9,807,340	(3,211,028)	-32.7%
Capital Grants and Contributions	1,039,379	1,910,070	(870,691)	-45.6%
Total Program Revenues	<u>7,861,508</u>	<u>11,765,283</u>	<u>(3,903,775)</u>	-33.2%
General Revenues and Special Items:				
Property taxes	4,964,099	5,138,708	(174,609)	-3.4%
Municipal license tax	6,595,907	5,727,821	868,086	15.2%
Sales taxes	272,665	0	272,665	273%
Other local taxes	1,083,462	999,331	84,131	8.4%
Grants and contributions not restricted to specific programs	3,162,396	3,063,894	98,502	3.2%
Interest and investment earnings	479,002	812,798	(333,796)	-41.1%
Miscellaneous	229,809	217,605	12,204	5.6%
Total General Revenues and Special Items	<u>16,787,340</u>	<u>15,960,157</u>	<u>827,183</u>	5.2%
Total Revenues	<u>24,648,848</u>	<u>27,725,440</u>	<u>(3,076,592)</u>	-11.1%
<b>EXPENSES</b>				
General government	5,321,795	5,488,033	989,403	-3.0%
Public safety	1,165,239	1,019,044	(399,357)	14.3%
Public works	5,820,806	4,256,599	938,335	36.7%
Health and welfare	6,277,781	5,718,465	158,166	9.8%
Culture and recreation	1,933,794	975,790	386,776	98.2%
Economic development	414,231	440,837	(82,097)	-6.0%
Community development	313,272	155,397	(292,133)	101.6%
Education	237,281	217,464	57,731	9.1%
Public lighting	918,039	852,608	(19,909)	7.7%
Interest on long-term debt	1,180,411	1,263,653	475,763	-6.6%
Total Expenses	<u>23,582,649</u>	<u>20,387,890</u>	<u>2,212,678</u>	15.7%
Change in net assets	<u>1,066,199</u>	<u>7,337,550</u>	<u>(5,289,270)</u>	-85.5%
Net assets (deficit) - beginning, as restated	9,315,467	2,182,182	7,133,285	326.9%
Net assets (deficit) - ending	<u>\$ 10,381,666</u>	<u>\$ 9,519,732</u>	<u>\$ 1,844,015</u>	9.1%

## FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

### Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$17,412,713 (\$15,817,741 in 2007) an increase of \$1,595,072 (\$3,526,427 in 2007) in comparison with the prior year. There are reservations of fund balance amounting to \$15,902,313 (\$14,888,593 in 2007). This is the fund balance that it is not available for new spending because it has already been committed 1) \$35,560 (\$137,085 in 2007) to liquidate contracts and purchase orders of the prior fiscal year, 2) \$3,103,905 (\$3,001,203 in 2007) to pay debt service, 3) \$12,308,142 (\$5,891,617 in 2007) to pay for capital projects and 4) \$454,706 (\$5,858,688 for 2007) for other purposes.

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2008, the general fund has an undesignated fund balance of \$1,510,500 (\$929,148, as restated in 2007).

### GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the Municipality Council revised the Municipality's budget in order to include increases in revenues that were identified during the course of the fiscal year based on current developments that positively affected the Municipality's finances. Increases in budgeted expenditures were also made since the law mandates a balanced budget.

The actual General Fund budgetary activities resulted in a favorable balance of \$491,685 (\$2,713,409 during the prior fiscal year), caused mainly due to savings in general government and public work expenditures.

### CAPITAL ASSETS AND DEBT ADMINISTRATION

#### Capital Assets

The Municipality has not maintained complete and adequate records related to the Capital Assets acquired and constructed in the past years, but the Municipality expects to compile documents and other information in the next fiscal years in order to attain complete and accurate records of its Capital Assets, and then, comply with such requirement. The Municipal Administration expects to develop a broad and comprehensive identification and assessments project of all fixed assets owned by the local government in order to capitalize them in its Statement of Net Assets, and then, reflects the correct net assets figure of the Municipality as a whole.

## **CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)**

The Municipality's investment in capital assets as of June 30, 2008, amounts to \$33,867,282 (\$30,087,837 in 2007), net of accumulated depreciation of \$12,017,601 (\$10,831,287 in 2007), including depreciation charges for the year totaled \$1,186,314 (\$1,022,230 in 2007), leaving a net book value of \$21,849,681 (\$19,256,551 in 2007). This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2008, the Municipality has \$6,282,617 (\$3,674,434 in 2007) of unexpended proceeds mainly from bond and notes issuances that are committed to future construction activities.

### **DEBT ADMINISTRATION**

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged.

The applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes such Municipality must have sufficient "payment capacity". Act No. 64 provides that a Municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, will be sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

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

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available but the revenue also is very predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2008-2009.

## **FINAL COMMENTS**

The Municipality is an autonomous governmental entity whose powers and authority vested on its Executive and Legislative Branches are specifically established in the Municipal Autonomous Act approved in August 1991. By virtue of such powers, it provides a wide range of services to its constituents which includes, among others, public works, education, public safety, public housing, health, community development, recreation, waste disposal, welfare and others. The Municipality's principal sources of revenues are derived from property taxes, municipal license taxes, subsidies from the Commonwealth of Puerto Rico's General Fund and contributions from the Traditional and Electronic Lottery sponsored by said Government.

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. Such has been the case of the financial operation corresponding to fiscal year 2008. It further contemplates to improve its current figure of net assets, which has been identified as one of the main short and long-term objectives of the Municipality.

## **FINANCIAL CONTACT**

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at P.O. Box 10, Peñuelas, Puerto Rico 00624-0010, or call (787) 836-1218.

**Commonwealth of Puerto Rico**  
**Municipality of Peñuelas**  
**Statement of Net Assets**  
**June 30, 2008**

	<b>Governmental Activities</b>
<b>Assets</b>	
Cash and cash equivalents	\$ 11,689,322
Cash with fiscal agent	9,326,474
Accounts receivable:	
Intergovernmental	812,584
Federal	946,915
Other	474,283
Capital assets	
Land, improvements, and construction in progress	3,743,268
Other capital assets, net of depreciation	18,106,413
Total capital assets	21,849,681
<b>Total assets</b>	<b>45,099,259</b>
 <b>Liabilities</b>	
Accounts payable and accrued liabilities	1,018,649
Due to other governmental entities	30,883
Claims and Judgments	
Deferred revenues:	
Municipal license tax	3,841,257
Federal grant revenues	902,500
Interest payable	777,363
Noncurrent liabilities:	
Due within one year	1,432,536
Due in more than one year	26,714,405
Total liabilities	<b>34,717,593</b>
 <b>Net Assets</b>	
Invested in capital assets, net of related debt	3,844,682
Restricted for:	
Capital projects	7,606,318
Debt service	2,326,542
Other purposes	5,192,090
Unrestricted (deficit)	(8,587,966)
<b>Total net assets</b>	<b>\$ 10,381,666</b>

Commonwealth of Puerto Rico  
Municipality of Peñuelas  
Statement of Activities  
For the Year Ended June 30, 2008

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 5,321,795	\$ -	\$ 10,075	\$ -	\$ (5,311,720)
Public safety	1,165,239	180,045		68,251	(916,943)
Public works	6,738,845	6,620	335,022	400,359	(5,996,844)
Health and welfare	6,277,781		4,878,805		(1,398,976)
Culture and recreation	1,933,793	39,152		188,165	(1,706,476)
Economic development	414,232		414,232		-
Community development	313,272		40,139	382,604	109,471
Education	237,281				(237,281)
Interest on long-term debt	1,180,411				(1,180,411)
<b>Total governmental activities</b>	<b>\$ 23,582,649</b>	<b>\$ 225,817</b>	<b>\$ 5,678,273</b>	<b>\$ 1,039,379</b>	<b>(16,639,180)</b>
General revenues and special items:					
Property taxes					4,964,099
Municipal license tax					6,595,907
Sales taxes					272,665
Other local taxes					1,083,462
Grants and contributions not restricted to specific programs					4,080,435
Interest and investment earnings					479,002
Miscellaneous					229,809
<b>Total general revenues</b>					<b>17,705,379</b>
Change in net assets					1,066,199
Net assets (deficit) - beginning, as restated					9,315,467
Net assets (deficit) - ending					<b>\$ 10,381,666</b>

Commonwealth of Puerto Rico  
Municipality of Peñuelas  
Balance Sheet  
Governmental Funds  
June 30, 2008

	General Fund	Special Revenue Fund Head Start	Capital Project Fund - Local, State & Federal Grants	Debt Service Fund	Peñuelas Development Fund	Special Revenue Fund - Local & State Grants	Other Governmental Funds	Total Governmental Funds
<b>Assets</b>								
Cash and cash equivalents	\$ 3,178,688	\$ 216,803	\$ 1,482,171	\$ -	\$ 4,701,824	\$ 1,338,163	\$ 771,673	\$ 11,689,322
Cash with fiscal agent	20,043		6,282,617	3,021,857		1,957		9,326,474
Accounts receivable:								-
Intergovernmental	452,591					266,847	946,915	1,666,353
Other	441,905			82,048				523,953
Due from other funds	1,782,539							1,782,539
<b>Total assets</b>	<b>\$ 5,875,766</b>	<b>\$ 216,803</b>	<b>\$ 7,764,788</b>	<b>\$ 3,103,905</b>	<b>\$ 4,701,824</b>	<b>\$ 1,606,967</b>	<b>\$ 1,718,588</b>	<b>\$ 24,988,641</b>
<b>Liabilities and Fund Balances</b>								
<b>Liabilities :</b>								
Accounts payable and accrued liabilities	\$ 457,566	\$ 73,366	\$ 72,682	\$ -	\$ -	\$ 277,070	\$ 137,965	\$ 1,018,649
Due to other governmental entities	30,883							30,883
Due to other funds		4,195	52,611			875,191	850,542	1,782,539
Deferred revenues:								
Municipal license tax	3,841,257							3,841,257
Federal grant revenues		139,242	33,177				730,081	902,500
<b>Total liabilities</b>	<b>4,329,706</b>	<b>216,803</b>	<b>158,470</b>	<b>-</b>	<b>-</b>	<b>1,152,261</b>	<b>1,718,588</b>	<b>7,575,828</b>
<b>Fund balances:</b>								
<b>Reserved for:</b>								
Encumbrances	35,560							35,560
Capital projects			7,606,318		4,701,824			12,308,142
Debt service fund				3,103,905				3,103,905
Other purposes						454,706		454,706
<b>Unreserved:</b>								
Undesignated	1,510,500							1,510,500
<b>Total fund balances</b>	<b>1,546,060</b>	<b>-</b>	<b>7,606,318</b>	<b>3,103,905</b>	<b>4,701,824</b>	<b>454,706</b>	<b>-</b>	<b>17,412,813</b>
<b>Total liabilities and fund balances</b>	<b>\$ 5,875,766</b>	<b>\$ 216,803</b>	<b>\$ 7,764,788</b>	<b>\$ 3,103,905</b>	<b>\$ 4,701,824</b>	<b>\$ 1,606,967</b>	<b>\$ 1,718,588</b>	<b>\$ 24,988,641</b>

Commonwealth of Puerto Rico  
Municipality of Peñuelas  
Statement of Revenues, Expenditures and Changes in Fund Balances  
Governmental Funds  
For the Year Ended June 30, 2008

	General Fund	Special Revenue Fund Head Start Program	Capital Project Fund - Local, State & Federal Grants	Debt Service Fund	Peñuelas Development Fund	Special Revenue Fund - Local & State Grants	Other Governmental Funds	Total Governmental Funds
<b>Revenues</b>								
Property taxes	\$ 3,815,474	\$ -	\$ -	\$ 1,148,625	\$ -	\$ -	\$ -	\$ 4,964,099
Municipal license taxes	6,595,907							6,595,907
Sales taxes	178,715			272,665				451,380
Licenses, permits and other local taxes	789,986				250,000			1,039,986
Charges for services	47,102							47,102
Intergovernmental	4,080,435		535,054			844,242		5,459,731
Interest	479,002							479,002
Federal grants		3,638,990					1,706,999	5,345,989
Miscellaneous	222,176							222,176
<b>Total revenues</b>	<b>16,208,797</b>	<b>3,638,990</b>	<b>535,054</b>	<b>1,421,290</b>	<b>250,000</b>	<b>844,242</b>	<b>1,706,999</b>	<b>24,605,372</b>
<b>Expenditures</b>								
<b>Current:</b>								
General government	4,949,176		28,156		128,816			5,106,148
Public safety	1,117,536		2,685		14,020			1,134,241
Public works	5,333,746		523,103		973,928	409,284	62,487	7,302,548
Health and welfare	1,051,788	3,638,990	82,807		468,084	76,942	1,171,743	6,490,354
Culture and recreation	1,458,055		1,164,233		468,236	613,067		3,703,591
Economic development						414,231		414,231
Community development					3,300	41,162	382,605	427,067
Education	218,379					3,330		221,709
<b>Debt service:</b>								
Principal				615,000				615,000
Interest				1,180,411				1,180,411
<b>Total expenditures</b>	<b>14,128,680</b>	<b>3,638,990</b>	<b>1,800,984</b>	<b>1,795,411</b>	<b>2,056,384</b>	<b>1,558,016</b>	<b>1,616,835</b>	<b>26,595,300</b>
Excess (deficiency) of revenues over (under) expenditures	2,080,117		(1,265,930)	(374,121)	(1,806,384)	(713,774)	90,164	(1,989,928)
<b>Other financing sources (uses)</b>								
Transfers in				476,823	3,516,716	617,138		4,610,677
Transfers out	(1,600,290)		(604,369)			(2,315,854)	(90,164)	(4,610,677)
Long-term debt issued			3,585,000					3,585,000
<b>Total other financing sources (uses)</b>	<b>(1,600,290)</b>	<b>-</b>	<b>2,980,631</b>	<b>476,823</b>	<b>3,516,716</b>	<b>(1,698,716)</b>	<b>(90,164)</b>	<b>3,585,000</b>
<b>Net change in fund balances</b>	<b>479,827</b>		<b>1,714,701</b>	<b>102,702</b>	<b>1,710,332</b>	<b>(2,412,490)</b>		<b>1,595,072</b>
Fund balance beginning, as restated	1,066,233		5,891,617	3,001,203	2,991,492	2,867,196		15,817,741
<b>Fund balance, ending</b>	<b>\$ 1,546,060</b>	<b>\$ -</b>	<b>\$ 7,606,318</b>	<b>\$ 3,103,905</b>	<b>\$ 4,701,824</b>	<b>\$ 454,706</b>	<b>\$ -</b>	<b>\$ 17,412,813</b>

*CAD 5/16/09*

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

**Commonwealth of Puerto Rico**  
**Municipality of Peñuelas**  
**Reconciliation of the Statement of Revenues,**  
**Expenditures, and Changes in Fund Balances of**  
**Governmental Funds to the Statement of Activities**  
**For the Year Ended June 30, 2008**

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**Net Change in Fund Balances - Total Governmental Funds** **\$ 1,595,072**

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

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period. 3,779,444

Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Change in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds. (1,186,314)

Interest expense on long-term debt was reported in the Government-Wide Statement of Activities and Change in Net Assets, but it did not require the use of current financial resources. Therefore, interest expense was not reported as expenditures in Governmental Funds. The following amount represented the change in accrued interest from prior year. (2,749)

Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long -term liabilities in the Government-Wide Statement of Net Assets. This is the amount paid in the current period 615,000

Repayment of claims and judgments debt is an expenditure in Governmental Funds, but the repayment reduces long -term claims and judgment debt in the Government-Wide Statement of Net Assets. This is the amount paid in the current period. 35,206

Accounts receivable not collected 60 days after the closing date are not recognized in Governmental Funds, but these receivables are reported in the Government-Wide statement of Net Assets. 43,476

Repayment of property tax debt is an expenditure in Governmental Funds, but the repayment reduces long -term property tax debt in the Government-Wide Statement of Net Assets. The following amount represent the change in long-term property tax debt from prior year. 43,948

Bonds and notes proceeds provide current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide statement of Net Assets. (3,585,000)

Repayment of retirement debt debt is an expenditure in Governmental Funds, but the repayment reduces long -term retirement debt in the Government-Wide Statement of Net Assets. The following amount represent the change in long-term retirement debt from prior year. (54,218)

Long-term compensated absences are reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represent the change in long-term compensated absences from prior year. (217,666)

**Change in Net Assets of Governmental Activities** **\$ 1,066,199**

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The Municipality of Peñuelas (the Municipality) is a local municipal government constituted in 1793 in the Commonwealth of Puerto Rico (the Commonwealth). The Municipality has full legislative, fiscal and all other governmental powers and responsibilities expressly assigned by Public Act No. 81 of August 30, 1991, as amended, known as *Autonomous Municipalities Act of the Commonwealth of Puerto Rico* (Act No. 81). The Municipality is one of seventy-eight municipalities legally separated from the Commonwealth's government.

The Commonwealth's Constitution provides for the separation of powers of the executive, legislative and judicial branches of the Commonwealth and the municipalities. However, the Municipality's governmental system consists of executive and legislative branches only. A Mayor, elected every four years by the citizens, exercises the executive power of the Municipality. The legislative power of the Municipality is exercised by the Municipal Legislature, whose members are also elected every four years. The judiciary power is exercised by the General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality.

The Municipality assumes either partial or full responsibility for providing services to its citizens related to public housing, welfare, public safety, health, sanitation, education, culture, recreation, education, urban development, economic development, and many other fiscal, general and administrative services.

The accounting policies and financial reporting practices of the Municipality conform to accounting principles generally accepted in the United States of America ("USGAAP") as applicable to governmental units.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

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

The following is a summary of the significant accounting policies of the Municipality:

**A. Component Units**

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, The Financial Reporting Entity, of the GASB, as amended by GASB Statement No. 39. 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 governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

**B. Government-wide and fund financial statements**

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

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

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

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

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The Municipality reports the following major governmental funds:

*General Fund*- is the accounting entity in which all governmental activity, except that which is required to be accounted for in another fund, is accounted for. Its revenues consist mainly of taxes, licenses and permits, intergovernmental revenue, charges for services and other.

*Special Revenue Fund – Head Start*- Is the accounting entity in which revenues derived from the federal agency are used to provide comprehensive health, educational, nutritional, social, and other developmental services primarily to economically disadvantaged preschool children (ages 3 to 5) and infants and toddler (birth through age 3) so that the children will attain school readiness.

*Capital Project Fund - Local, State and Federal Grants* - is the accounting entity in which revenues derived from local funds, state and federal grants or other restricted revenue sources related to capital projects, is accounted for. The uses and limitations of each capital project fund are specified by Municipality ordinances or federal and state statutes.

*Debt Service Fund* - is the accounting entity used to account for the resources accumulated and payments made for principal and interest on long-term general obligation bonds of governmental funds.

*Peñuelas Development Fund* - is the accounting entity in which revenues derived from tax investigations related to municipal licenses and construction excise taxes, and residual equity from other inactive funds are accounted for, principally to be used for capital projects. The uses and limitations of the fund are specified by Municipality ordinances and Executive resolutions.

*Special Revenue Fund – Local and State Grants* - is the accounting entity in which revenues derived from local funds and state grants or other restricted revenue sources is accounted for the uses and limitations by Municipality ordinances or state statutes.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

*Other Governmental Funds* - is the accounting entity in which revenues derived from local funds, state grants, federal grants or other restricted revenue source, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or state and federal statutes.

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

C. Financial reporting presentation

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

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

*Special Revenue Fund - Head Start* - Is the accounting entity in which revenues derived from the federal agency are used to provide comprehensive health, educational, nutritional, social, and other developmental services primarily to economically disadvantaged preschool children (ages 3 to 5) and infants and toddler (birth through age 3) so that the children will attain school readiness.

*Capital Projects Funds - Local, State and Federal Grants* - Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

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

*Peñuelas Development Fund* - is the accounting entity in which revenues derived from tax investigations related to municipal licenses and construction excise taxes, and residual equity from other inactive funds are accounted for, principally to be used for capital projects. The uses and limitations of the fund are specified by Municipality ordinances and Executive resolutions.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

*Other Funds– Local, State and Federal Grants* - is the accounting entity in which revenues derived from local funds, state and federal grants or other restricted revenue sources are accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

D. Measurement focus, basis of accounting and financial presentation

Except for budgetary purposes, the basis of accounting used by the Municipality conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The Municipality has elected not to apply all Statements and Interpretations issued by the Financial Accounting Standard Board after November 30, 1989, in accordance with GASB Statement No. 20.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures when payment is due. General capital asset acquisitions are reported as expenditure in governmental funds. Proceeds from issuance of general long-term debt reported as other financing sources.

Property taxes, franchise taxes, licenses, rent, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash. Private-sector standards of accounting and financial reporting issue prior to December 1, 1989,

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

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

generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants, and contributions, and 3) capital grants and contributions, including special assessments, if any. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources, as they are needed.

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**E. Assets, liabilities and net assets**

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

Cash with fiscal agent in the debt services fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law.

2. **Receivables and payables-** Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables in the General Fund represents mostly contributions from the Puerto Rico Electric Power Authority (PREPA), which, pays the municipalities as contributions in lieu of taxes greater of the following amounts: (a) twenty percent (20%) of its net revenues as defined in the Trust Indenture signed with the Trustee as representative of the bondholders, adjusted by subsidies granted by the PREPA; (b) an amount equal to the actual cost of electric power consumed by each Municipality in its common facilities during the current year; or (c) an average of the contribution in lieu of taxes paid by PREPA to each municipality during the past five fiscal years. The contribution in lieu of tax revenue recorded in the General Fund for the current fiscal year was determined based on expenditures actual transactions during the current fiscal year, because the final contribution amount from the PREPA was not available at the date of release of the basic financial statements. Intergovernmental receivable in the special revenue or capital project funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded or state funded programs.

3. **Inventories-** Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.
4. **Capital assets-** Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

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

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Buildings and site improvements	40 years	\$1
Infrastructure	40 years	\$1
Works of art	10 years	\$1
Vehicles	5 years	\$1
Furniture and fixtures	5 years	\$25
Machinery and equipment	3 to 5 years	\$25

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

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

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

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality.

7. Claims and judgments- The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.
8. Reservation of fund balance- Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:

- a. *Capital Projects*- Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

- b. committed amounts generally will become liabilities in future periods as the projects are completed.
  - c. *Encumbrances*- Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
  - d. *Other Purposes*- Represents net assets available for specific use and/or legally segregated for other specific future use.
  - e. *Debt Service Fund*- Represents net assets available to finance future debt service payments.
9. Interfund and intra-entity transactions- The Municipality has the following types of transactions among funds:
- a. *Operating Transfers*- Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
  - b. *Intra-Entity Transactions*- Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
10. *Risk financing*- The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2008 amounted to approximately \$169,646. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$369,562 for workers compensation insurance covering all municipal employees.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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

11. Reconciliation of Government-wide and Fund Financial Statements

The governmental fund balance sheet includes reconciliation between fund balance-total governmental funds and net assets-governmental activities as reported in the government-wide statement of net assets. The two elements of that reconciliation explains that "long term liabilities, including compensated absences, bonds and notes payable, are not due and payable in the current period and therefore are not reported in the funds.", and that "capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. The details of this reconciliation are as follows:

		<u>Total Net Assets</u> <u>Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 21,849,681	
Deduct:		
Bonds Payable	<u>(18,005,000)</u>	<u>\$ 3,844,682</u>
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		7,606,318
<u>Net assets restricted for debt service</u>		
Debt service fund - fund balance	\$3,003,905	
Deduct:		
Interest payable	<u>(777,363)</u>	2,326,542
<u>Net assets restricted for other purposes</u>		
Special revenue fund - local and state grants restricted		5,192,090
<u>Net assets unrestricted (deficit)</u>		
General fund - total fund balance:	\$1,546,060	
Add: Unavailable Accounts Receivables	43,476	
Deduct:		
Retirement Administration Debt	(208,813)	
Bonds Payable	(6,116,000)	
Property Tax Debt	(1,907,350)	
Compensated Absences	(1,869,353)	
Claims and judgment debts	<u>(40,426)</u>	<u>(8,587,966)</u>
Total net assets - governmental activities		<u>\$ 10,381,666</u>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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**2. DEPOSITS**

Under Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The Municipality's bank balances in commercial banks of approximately \$3,178,688 in the general fund, \$216,803 in the special revenue fund – head start, \$1,482,171 in the capital project fund – local, state and federal grants, \$4,701,824 in the Peñuelas development fund \$1,338,163 in the special revenue fund – local and state grants were fully collateralized at June 30, 2008. In the other governmental funds there were deposits with commercial banks of approximately \$771,673 that were fully collateralized.

The deposits at GDB of approximately \$20,043, that is restricted for other purposes in the general fund, the \$1,957 in the special revenue fund – local and state grants, the \$6,282,617 that is restricted principally for capital projects in the capital project fund – local, state and federal grants, and the \$3,021,857 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

**3. RECEIVABLES**

A. *Municipal License Tax*- The Municipality impose a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2008, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues
2. Other organizations- 0.40% of gross revenues

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2008, net of allowance for uncollectible.

Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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3. RECEIVABLES (CONTINUED)

A. *Intergovernmental Receivables*- Intergovernmental receivables of \$452,591 in the General Fund principally consist of the amounts due from CRIM resulting from the excess of current year property tax collections over current year advances:

Intergovernmental receivable of \$266,847 in the special revenue fund – local and state grants represent expenditures incurred not yet reimbursed by Department of Labor – Law 52 and 82 Grants.

Intergovernmental receivable in other governmental funds represent expenditures incurred not yet reimbursed by the Federal government or the pass-through grantor. Following is a detail of the intergovernmental receivable:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grant	\$ 899,940
Public Assistance Grant	15,267
Edward Byrne Memorial	552
Homeland Security	28,712
Hazard Mitigation	<u>1,444</u>
Total	<u>\$ 946,915</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

**4. INTERFUND TRANSACTIONS**

Interfund receivables and payables at June 30, 2008, and interfund transfers during the fiscal year ended at June 30, 2008, are summarized as follows:

**a. Due from/to other fund:**

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund – Local and State Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	\$ 875,191
General Fund	Special Revenue Fund – Head Start	Payroll and related accruals paid and not reimbursed.	4,195
General Fund	Capital Project Fund – Local, State and Federal Grants	Reimbursable expenditures	52,611
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	<u>850,542</u>
<b>Total</b>			<b><u>\$ 1,782,539</u></b>

**b. Transfer in/out to other fund**

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Debt Service Fund	Debt retirement	\$ 476,823
General Fund	Peñuelas Development Fund	Public works, health and welfare and cultural and recreation investments	1,008,999
General Fund	Special Revenue Fund – Local and State Grants	Public works	114,468
Capital Project Fund – Local, State and Federal Grants	Peñuelas Development Fund	Public works, health and welfare and cultural and recreation investments	604,369
Special Revenue Fund – Local and State Grants	Peñuelas Development Fund	Public works, health and welfare and cultural and recreation investments	1,813,184
Other Governmental Funds	Peñuelas Development Fund	Public works, health and welfare and cultural and recreation investments	90,164
Special Revenue Fund – Local and State Grants	Special Revenue Fund – Local and State Grants	Public works, health and welfare and cultural and recreation investments	<u>502,670</u>
<b>Total</b>			<b><u>\$ 4,610,677</u></b>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

**5. CAPITAL ASSETS**

Capital assets; those with an estimated useful live of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2008, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<u>Governmental Activities:</u>	<u>Balance</u> <u>July 1, 2007</u>	<u>Additions</u>	<u>Transfers</u>	<u>Balance</u> <u>June 30, 2008</u>
Capital asset, not being depreciated:				
Land	\$ 659,123			\$ 659,123
Construction in progress	<u>3,299,823</u>	<u>\$ 3,084,145</u>	<u>\$ (3,299,823)</u>	<u>3,084,145</u>
Total capital assets not being depreciated	<u>\$ 3,958,946</u>	<u>\$ 3,084,145</u>	<u>\$ (3,299,823)</u>	<u>\$ 3,743,268</u>
Capital assets, being depreciated:				
Buildings	\$10,783,511		\$ 2,757,078	\$ 13,540,589
Buildings improvements				
Infrastructure	8,732,151		542,745	9,274,896
Infrastructure improvements	228,502			228,502
Equipment	1,540,128	\$ 284,338		1,824,466
Furnishing				
Computers				
Vehicles	<u>4,844,600</u>	<u>410,961</u>	<u>-</u>	<u>5,255,561</u>
Total capital assets being depreciated	<u>\$ 26,128,892</u>	<u>\$ 695,299</u>	<u>\$ 3,299,823</u>	<u>\$ 30,124,014</u>
Less accumulated depreciation for:				
Buildings	\$ (3,247,262)	\$ (437,451)		\$ (3,684,713)
Buildings improvements				
Infrastructure	(2,981,621)	(305,557)		(3,287,178)
Infrastructure improvements	(127,212)	(10,243)		(137,455)
Equipment	(1,213,906)	(93,854)		(1,307,760)
Furnishing				
Computers				
Vehicles	<u>(3,261,285)</u>	<u>(339,209)</u>	<u>-</u>	<u>(3,600,494)</u>
Total accumulated depreciation	<u>\$(10,831,287)</u>	<u>\$(1,186,314)</u>	<u>\$ -</u>	<u>\$(12,017,601)</u>
Total capital assets being depreciated, net	<u>\$ 15,297,605</u>	<u>\$ (491,014)</u>	<u>\$ 3,299,823</u>	<u>\$ 18,106,413</u>
Governmental activities capital assets, net	<u>\$ 19,256,551</u>	<u>\$ 2,593,131</u>	<u>\$ -</u>	<u>\$ 21,849,681</u>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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5. CAPITAL ASSETS (CONTINUED)

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

Governmental activities:

General government	\$ 473,121
Public safety	26,895
Public works	393,886
Culture and recreation	221,536
Education	13,396
Health and welfare	<u>22,733</u>
Total depreciation expense-governmental activities	<u>\$ 1,186,314</u>

6. PROPERTY TAXES

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

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

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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**6. PROPERTY TAXES (CONTINUED)**

On January 26, 2000, Public Law 42 was enacted which authorized the CRIM to obtain a loan up to \$200,000,000, and for a term not to exceeding 10 years, to allow for the financing of the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections through fiscal year ended June 30, 2000. The amounts that the Municipalities will collect from additional property taxes resulting from increases in the subsidy from the Commonwealth of Puerto Rico to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law 238, enacted on August 15, 1999. On October 11, 2001, Public Law 146 was enacted to amend Public Law 42, to extend the loan amortization period up to 30 years.

Also, on October 11, 2002, Public Law 172 was enacted, to provide as an option for the Municipalities to include the debt that the Municipalities of Puerto Rico have with the CRIM arising from final settlements of property tax advances versus actual collections for the fiscal year ended June 30, 2001 with the loan authorized through Public Law 42 enacted on January 26, 2000.

On June 26 1997, Public Law Num. 21 was enacted authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable or equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities thru a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law.

The government-wide statement of net assets includes an outstanding debt balance of \$1,351,351 and \$555,999 related to Law 42 and Law 146, respectively at June 30, 2008.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

6. PROPERTY TAXES (CONTINUED)

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

The annual tax rate is 8.33% for real property and 6.33% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.50% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

7. DUE TO OTHER GOVERNMENTAL ENTITIES:

The amounts due to other governmental entities in the general fund include the following:

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Aqueduct and Sewer Authority	\$ 29,584
General Services Administration	<u>1,299</u>
Total	<u>\$ 30,883</u>

8. DEFERRED REVENUES

- A. Municipal License Tax- The deferred revenues of approximately \$3,841,257 in the general fund relates to municipal license tax collected in fiscal year 2007-08 that will be earned in fiscal year 2008-09.

Federal Government- The deferred revenues presented in the special revenue fund - head start represents the portion of federal grant received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Head Start Program	\$ 91,285
Child and Adult Care Food Program	<u>47,957</u>
Total	<u>\$ 139,242</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

**8. DEFERRED REVENUES (CONTINUED)**

The deferred revenues presented in the capital project funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Rural Development	<u>\$ 33,177</u>
Total	<u>\$ 33,177</u>

The deferred revenues presented in the other governmental funds represent the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

<u>Program Description</u>	<u>Amount</u>
Emergency Management - State and Local Assistance	\$ 3,629
Public Assistance Grant	46,376
Section 8 Housing Choice Voucher	678,148
Others	<u>1,928</u>
Total	<u>\$ 730,081</u>

**9. LONG-TERM LIABILITIES**

Long-term liability activity for the year ended June 30, 2008, was as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds Payable	\$21,151,000	\$3,585,000	\$ (615,000)	\$24,121,000	\$ 680,000
Property Tax Debt	1,951,298	70,376	(114,324)	1,907,350	184,701
Treasury Department-Claims	75,631		(35,206)	40,425	35,207
Compensated Absences	1,651,687	1,446,709	(1,229,043)	1,869,353	375,326
Retirement Debt	<u>154,595</u>	<u>105,729</u>	<u>(51,511)</u>	<u>208,813</u>	<u>167,302</u>
Total	<u>\$24,984,211</u>	<u>\$5,207,814</u>	<u>\$(2,045,084)</u>	<u>\$28,146,941</u>	<u>\$1,432,536</u>

1. Legal debt margin- The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment of property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds and notes payable, is paid with unrestricted funds.

**COMMONWEALTH OF PUERTO RICO  
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**NOTES TO BASIC FINANCIAL STATEMENTS  
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**9. LONG-TERM LIABILITIES (CONTINUED)**

2. Bonds payable- The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. Bonds payable outstanding at June 30, 2008 are as follows:

<u>Type of bonds</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest Rates</u>	<u>Balance at June 30, 2008</u>
1999-Series	7-1-2018	\$ 2,630,000	5.00% to 7.81%	\$ 1,945,000
2000-Series	7-1-2026	1,760,000	5.00% to 7.00%	1,315,000
2001-Series	7-1-2010	1,300,000	5.00% to 8.00%	1,085,000
2001-Series	7-1-2017	1,070,000	5.00% to 8.00%	795,000
2002-Series	7-1-2026	135,000	5.00% to 7.00%	105,000
2002-Series	7-1-2021	475,000	5.00% to 7.00%	395,000
2002-Series	7-1-2026	1,965,000	5.00% to 7.00%	1,740,000
2002-Series	7-1-2026	2,085,000	5.00% to 7.00%	1,795,000
2004-Series	7-1-2027	1,115,000	5.00% to 6.50%	1,010,000
2004-Series	7-1-2014	1,195,000	5.00%	895,000
2005-Series	7-1-2030	1,730,000	5.00%	1,655,000
2005-Series	7-1-2030	3,021,000	5.00%	3,006,000
2005-Series	7-1-2030	3,685,000	5.00%	3,455,000
2006-Series	7-1-2030	1,390,000	6.25% to 7.25%	1,340,000
2008-Series	7-1-2032	1,585,000	3.93% to 7.50%	1,585,000
2008-Series	7-1-2032	2,000,000	3.93% to 7.50%	<u>2,000,000</u>
Total general obligation bonds				<u>\$ 24,121,000</u>

These bonds, except the \$1,760,000 Bonds 2000 Series, \$ 2,085,000 Bonds 2002 Series and the \$3,021,000 Bonds 2005 Series, are payable from the ad valorem property tax of 1.50% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

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

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2009	\$ 680,000	\$ 1,305,995
2010	765,000	1,423,904
2011	805,000	1,375,977
2012	855,000	1,324,942
2013	920,000	1,275,652
2014-2018	5,515,000	5,432,295
2019-2023	6,465,000	3,883,410
2024-2028	6,095,000	2,164,675
2029-2032	<u>3,021,000</u>	<u>668,850</u>
Total	<u>\$ 24,121,000</u>	<u>\$ 18,855,700</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

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**9. LONG-TERM LIABILITIES (CONTINUED)**

3. **Property Tax Debt-** These amounts represent the balance owned to the Treasury Department and to the Municipal Revenue Collection Center (CRIM) at June 30, 2008 as described in Note 6.
4. **Treasury Department Debt-** These amounts represent the balance owned to the Treasury Department at June 30, 2008, for payments of claims and judgments to third parties disbursed by the Treasury Department and related to claims and judgments unfavorable outcomes or final settlements against the Municipality. The Municipality agreed with the treasury Department to reimburse to it such amount in monthly installments to be retained by the Municipal Revenue Collection Center from the monthly property tax advances.
5. **Compensated absences-** The government-wide statement of net assets includes approximately \$1,168,916 of accrued sick leave benefits, and approximately \$700,437 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

**10. PENSION PLAN**

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple defined benefit pension plan sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement

COMMONWEALTH OF PUERTO RICO  
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NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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10. PENSION PLAN (CONTINUED)

benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

Members who have attained 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have completed ten years of creditable service are entitled to an annual benefit payable monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation, as defined, multiplied by the number of years of creditable service up to twenty years, plus two percent of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined; otherwise they will receive 75 percent of the average compensation, as defined. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$ 550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total employee and employer contributions during the year ended June 30, 2008 amounted to approximately \$330,191 and \$370,094, respectively.

On September 24, 1999, an amendment to Act. No. 447 of May 15, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employee's participation in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 1, 2000, will only be allowed to become members of System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees),

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**NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008**

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**10. PENSION PLAN (CONTINUED)**

or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances.

Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2008, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940.

**11. RISK MANAGEMENT**

The Finance Department is responsible of assuring that the Municipality's property is properly insured. Annually, the Finance Department Division compiles the information of all property owned and its respective market value. After evaluating this information, the Finance Department Division submits the data regarding the Municipality's properties to the Public Insurance Department at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities.

**12. CAPITAL ASSETS REPORTED VALUE**

The Municipality has not maintained complete and adequate records related to the Capital Assets reported in governmental activities of the government-wide financial statements and, therefore, such condition would affect the amounts of assets, net assets, and expenses of the governmental activities. The Municipality expects to compile documents and other information in the next fiscal years in order to attain complete and accurate records of its Capital Assets.

**13. CONTINGENCIES**

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities. It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

The Municipality participates in a number of federal financial assistance programs funded by the Federal Government. Expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantor. The amount, if any, of expenditures which may be disallowed by such audits cannot be determined at this time, although the Municipality management expects such amounts, if any, will not be material.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BASIC FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2008

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**14. RESTATEMENTS**

The beginning Governmental Activities Net Assets has been restated by approximately \$49,670 to properly present the previously reported net assets at June 30, 2007. The restatement is mainly due to the correction of the other accounts receivable balance erroneously reported.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF PEÑUELAS**  
**BUDGETARY COMPARISON SCHEDULE- GENERAL FUND**  
**(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)**  
**YEAR ENDED JUNE 30, 2008**

	<u>Budgeted Amounts</u>		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
<b>REVENUES AND OTHER FINANCING SOURCES:</b>				
Property taxes	\$ 3,597,199	\$ 3,597,199	\$ 3,536,047	\$ (61,152)
Municipal license tax	5,208,486	6,577,962	6,578,830	868
Licenses, permits and other local taxes	191,000	860,040	649,249	(210,791)
Charges for service	33,000	33,000	47,572	14,572
Intergovernmental	4,089,761	4,089,761	4,080,435	(9,326)
Interest	250,000	593,000	537,042	(55,958)
Miscellaneous	<u>35,000</u>	<u>45,800</u>	<u>85,708</u>	<u>39,908</u>
Total revenues and other financing sources	<u>13,404,446</u>	<u>15,796,762</u>	<u>15,514,883</u>	<u>(281,879)</u>
<b>EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:</b>				
Current:				
General government	4,258,105	5,095,805	4,661,608	434,197
Public safety	5,063,175	5,429,675	5,168,575	261,100
Public works	1,170,220	1,094,138	1,087,226	6,912
Health and welfare	1,110,908	1,087,230	1,057,274	29,956
Culture and recreation	1,048,271	1,376,794	1,359,158	17,636
Education	198,317	212,670	212,534	136
Operating transfer to other funds	<u>555,450</u>	<u>1,500,450</u>	<u>1,476,823</u>	<u>23,627</u>
Total expenditures, encumbrances and other financing uses	<u>\$ 13,404,446</u>	<u>\$ 15,796,762</u>	<u>15,023,198</u>	<u>773,564</u>
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)</b>				
	-	-	<u>\$ 491,685</u>	<u>\$ 491,685</u>
<b>Explanation of Differences:</b>				
<b>Sources/inflows of resources:</b>				
Actual amounts (budgetary basis)"available for appropriation" from the budgetary comparison schedule				\$ 15,514,883
Differences-budget to GAAP:				
No budgeted revenues				<u>693,914</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 16,208,797</u>
<b>Uses/outflows of resources:</b>				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$ 15,023,198
Differences-budget to GAAP:				
Net change in encumbrances				101,525
GAAP adjustments to expenditures				<u>604,247</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 15,728,970</u>

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO BUDGETARY COMPARISON SCHEDULE- GENERAL FUND  
YEAR ENDED JUNE 30, 2008

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1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

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

The Municipality prepares its annual budget including the operations of the general fund.

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2008 representing the original budget. There were supplemental appropriations for the year ended June 30, 2008.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

**YEAR ENDED JUNE 30, 2008**

<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>
<b>U.S. DEPARTMENT OF AGRICULTURE:</b>			
Pass-through the Commonwealth of Puerto Rico - Department of Education: Child and Adult Care Food Program	10.558	Not Available	\$ <u>257,244</u>
Total U.S. Department of Agriculture			<u>257,244</u>
<b>U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:</b>			
Direct Program: Section 8 Housing Choice Vouchers	14.871		840,505
Pass-through the Commonwealth of Puerto Rico - Office of the Commissioners of Municipal Affairs: Community Development Block Grant / Small Cities	14.228	Not Available	<u>382,605</u>
Total U.S. Department of Housing and Urban Development			<u>1,223,110</u>
<b>U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES</b>			
Pass-through the Communal Services Institute: Community Services Block Grant	93.569	Not Available	8,868
Pass-through the Commonwealth of Puerto Rico - Administration for Children and Families: Head Start Program	93.600	Not Available	<u>3,381,746</u>
Total U.S. Department of Health and Human Services			<u>3,390,614</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)**

**YEAR ENDED JUNE 30, 2008**

<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>
<b>U.S. DEPARTMENT OF HOMELAND SECURITY</b>			
Pass-through the Commonwealth of Puerto Rico Governor Office - Public Security Affairs Office:			
Homeland Security Grant Program	97.067	Not Available	62,357
Pass-through the Commonwealth of Puerto Rico - Governor Authorized Representative (GAR):			
Public Assistance Grant	83.544	Not Available	<u>27,352</u>
Total U.S. Department of Homeland Security			<u>89,709</u>
<b>TOTAL EXPENDITURES OF FEDERAL AWARDS</b>			<u><u>\$ 4,960,677</u></u>

The accompanying notes are an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF PEÑUELAS

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2008

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**1. BASIS OF PRESENTATION:**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Municipality of Peñuelas, Commonwealth of Puerto Rico (the Municipality) for the fiscal year ended June 30, 2008. The Municipality's reporting entity is disclosed in Note 1 to the Municipality's basic financial statements as of and for the fiscal year ended June 30, 2008.

The accompanying schedule of expenditures of federal awards is presented on the modified accrual basis of accounting.

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*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statement.



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

To the Honorable Mayor and  
Members of the Municipal Legislature  
MUNICIPALITY OF PEÑUELAS, PUERTO RICO

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Peñuelas, Puerto Rico (the "Municipality") as of and for the fiscal year ended June 30, 2008, which collectively comprise Municipality of Peñuelas's basic financial statements and have issued our report thereon dated December 8, 2008. The report on governmental wide financial statement was adverse because not maintained complete and adequate records in order to obtain sufficient and competent evidential matter related to the Capital Assets reported in the governmental activities. 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.

Internal Control Over Financial Reporting

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

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Municipality's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of Municipality's financial statements that is more than inconsequential will not be prevented or detected by Municipality's internal control. We consider the deficiencies described in the accompanying schedule of finding and questioned costs to be significant deficiencies in internal control over report. See finding 08-01 and 08-02.

## INDEPENDENT AUDITORS' REPORT

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider 08-01 to be material weakness.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's 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 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 instances of noncompliance or other matter that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items 08-01 and 08-02.

Municipality's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit Municipality's response and, accordingly, we express no opinion on it.

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

*Mendoza & Ramos CPAs*  
MENDOZA & RAMOS  
CERTIFIED PUBLIC ACCOUNTANTS, C.S.P.

Guayama, Puerto Rico  
February 24, 2009

Stamp number 2395335 was  
affixed to the original of this  
report.





**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  
Members of the Municipal Legislature  
MUNICIPALITY OF PEÑUELAS, PUERTO RICO

Compliance

We have audited the compliance of the Municipality of Peñuelas, Puerto Rico (the "Municipality") 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 fiscal year ended June 30, 2008. The Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on the Municipality's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Municipality's compliance with those requirements and performing such others 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's compliance with those requirements.

As described item 08-03, 08-04, 08-05, 08-06, 08-07, 08-08, 08-09 and 08-10 in the schedule of findings and questioned costs, the Municipality did not comply with requirements regarding Allowable Cost, Cash Management, Procurement, Suspension and Debarment, Reporting and Special Test that are applicable to its Community Development Block Grant Program. Compliance with such requirements is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

## INDEPENDENT AUDITORS' REPORT

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As described item 08-11 in the schedule of findings and questioned costs, the Municipality did not comply with requirements regarding Cash Management that are applicable to its Section 8 Housing Choice Vouchers. Compliance with such requirements is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

As described item 08-12 and 08-13 in the schedule of findings and questioned costs, the Municipality did not comply with requirements regarding Allowance Costs and Reporting are that are applicable to its Head Start Program. Compliance with such requirements is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the Fiscal Year Ended June 30, 2008.

### Internal Control Over Compliance

The management of the Municipality 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's internal control over compliance with the 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality's internal control over compliance.

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

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Municipality's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of federal program that is more than inconsequential will not be prevented or detected by the Municipality's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of finding and questioned costs as items 07-09 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by Municipality's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of finding and questioned costs, we consider items 07-09 to be material weaknesses.

INDEPENDENT AUDITORS' REPORT

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Municipality's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Municipality's response and, accordingly, we express no opinion on it.

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

*Mendoza & Ramos CPA's*  
MENDOZA & RAMOS  
CERTIFIED PUBLIC ACCOUNTANTS, C.S.P.

Guayama, Puerto Rico  
February 24, 2009

Stamp number 2395336 was  
affixed to the original of this  
report.



**FINDINGS AND QUESTIONED COST:**

- Schedule of Findings and Questioned Costs
- Summary Schedule of Prior Audit Findings

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION I-FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Financial Statements

Type of auditors' report issued:

- Unqualified Opinion, except for adverse opinion for government-wide financial statement
- Qualified Opinion
- Adverse Opinion
- Disclaimer Opinion

Internal control over financial reporting:

- Material weakness (es) identified?  Yes  No
- Significant deficiencies identified that are not considered to be material weakness (es)?  Yes  None Reported
- Noncompliance material to financial statements noted?  Yes  No

Federal Awards

Internal control over major programs:

- Material weakness (es) identified?  Yes  No
- Significant deficiencies identified that are not considered to be material weakness (es)?  Yes  None Reported

Type of auditors' report issued on compliance for Major Programs:

- Unqualified Opinion
- Qualified Opinion
- Adverse Opinion
- Disclaimer

Any audit findings disclosed that are required to be reported in accordance with 510(a) OMB Circular A-133?

- Yes  No

The Municipality's major programs were:

CFDA Number	Name of Federal Program
14.228	Community Development Block Grant
14.871	Section 8 Housing Choice Vouchers
93.600	Head Start Program

Dollar threshold used to distinguish between Type A and Type B Programs:

\$300,000

Auditee qualified as low-risk auditee?

- Yes  No

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION II – FINANCIAL STATEMENT FINDINGS

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FINDING	08-01
CATEGORY	INTERNAL CONTROL
NONCOMPLIANCE	CAPITAL ASSETS
TOPIC SENTENCE	Fixed \ Capital Assets and Expenditures – Subsidiary Ledger.
CONDITION	The Municipality has not maintained complete and adequate records in order to obtain sufficient, competent evidential matter with respect to the Capital Assets reported in governmental activities and, accordingly, the amount by which this departure would affect the assets, net assets, and expenses of the governmental activities is not determinable.
CRITERIA	Chapter IX, Article 9.002 of State Act Number 81 of August 30, 1991 states that the municipality should maintain updated property accounting records. Also the GASB Statements No. 34 requires that all capital assets, including infrastructure, must be presented in the Statements of Net Assets and that these assets must be depreciated during its useful life.
CAUSE	Competent and sufficient evidential matter related to the capital assets was not available to support the value, completeness and ownership of these assets.
EFFECT	The Municipality's Government Wide Financial Statements do not present fairly, the financial position of the governmental activities, and the change in financial position of the Municipality.
RECOMMENDATION	We recommend that the Municipality should continue the compilation of documents to support the value, completeness and ownership of its capital assets, to comply with the requirements of the GASB Statement No. 34.
QUESTIONED COSTS	NONE
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Now, the Municipality's Finance Department staffs continue updating the capital assets subsidiary ledger in order to comply with the GASB No. 34 capital assets requirements for the fiscal year ended on June 30, 2009.  Implementation Date: June 30, 2009 Responsible Person: Mr. Arnaldo Rivera, Finance Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION II – FINANCIAL STATEMENT FINDINGS

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FINDING	08-02
CATEGORY	INTERNAL CONTROLS
TOPIC SENTENCE	ACCOUNTING SYSTEM
CONDITIONS	The accounting system and manuals used by the Municipality to account and register the financial transactions during the fiscal year does not provide for the summarization of transactions that permit the preparation of Municipality's financial statements in conformity with the General Accepted Accounting Principals of the United States of America (GAAP).
CRITERIA	According to Article 8.010 (a) and (b) of Law Num. 81 for the Municipalities of Puerto Rico, the computerized system and the procedures of accounting and property will be design so that it allows the Municipality to carry out its functions, at the same time as they serve to maintain an uniform and coordinated accounting, that provide a complete picture of the financial operations of the Municipality and the necessary financial information that assist the Municipality Legislature, the Governor, and the Secretary of the Puerto Rico Treasury Department in the performance of its respective responsibilities. Municipalities accounting will be based on funds, Generally Accepted Accounting Principles and the requirements established by the Governmental Accounting Standard Board. Also the pronouncements of the National Committee on Governmental Accounting and the "Blue Book" will be used to design municipalities' accounting systems and fiscal procedures.
CAUSES	Municipality's accounting system and financial reports are subject to State's agencies requirements which does not allow nor provide the Municipality with the necessary tools capable of recapturing the financial information and provide financial statements.
EFFECT	The lack of an adequate accounting system which can captures all the financial information and generates Municipality's financial statements for each fiscal year affect the Municipality ability to measure the financial and nonfinancial performance of programs and activities; adequately safeguard significant assets and properly record various transactions; and hinder the Municipality from having reliable financial information to operate in an economical, efficient, and effective manner.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION II – FINANCIAL STATEMENT FINDINGS

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Sound decisions on the current results and future direction of vital programs and policies are made more difficult without timely, reliable and useful financial performance information.

RECOMMENDATION

The Municipality should establish and implement the necessary measures that allow the summarization of the financial transactions in order to prepare the financial statements in conformity with GAAP.

QUESTIONED COSTS

None

MANAGEMENT RESPONSE  
AND CORRECTIVE ACTION PLAN

The Office of the Commissioner of Municipal Affairs is considering alternatives to for the acquisition of new accounting software, and therefore, we will hope to solve our accounting system condition in a near future. But in a short term, we implemented the Peachtree accounting software as an alternate tool in order to maintain monthly reconciled records of all of our funds.

Implementation Date: June 30, 2010

Responsible Person: Mr. Arnaldo Rivera  
Finance Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-03
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	COMPLIANCE
NONCOMPLIANCE	ALLOWABLE COSTS / COST PRINCIPLES
TOPIC SENTENCE	Unallowable costs
CONDITIONS	<p>During the fiscal year 2007-2008, the Program paid to each “Ama de Llaves” 3.33 hours in excess of the amount of hours worked during a bi-weekly period. Such amount of hours were also in excess of the amount of hours authorized to be pay to each “Ama de Llaves” per Program’s annual proposal submitted to and authorized by the Lead Agency (OCAM).</p> <p>In addition, the amount of funds invoiced from and paid to the Municipality regarding the amounts previously paid by the Municipality to each “Ama de Llaves” does not agree to the payroll reports.</p>
CRITERIA	<p>As stated in 24 CFR 85.22(a) grant funds may be used only for the allowable costs of the grantees. OMB Circular A-87, Attachment A, C. 1 and 3 established that to be allowable under Federal awards a cost must: (c) be authorized or not prohibited under State or local laws or regulations; (j) adequately documented. A cost is allocable to a particular cost objective if the goods or services involved are chargeable or assignable to such cost objective in accordance with relative benefits received.</p>
CAUSE	<p>The aforementioned conditions were caused since payments were made according to Program’s annual estimate and budget of work hours and days and not to actual amount of hours and days worked by each “Ama de Llaves”.</p>
EFFECT	<p>Incurring in unallowable costs result in questioned costs and the reimbursements of funds to the federal government. In addition, the Municipality could be subject to penalties from the Federal Government and be adversely affected in the benefits they are entitled to receive in the future.</p>

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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**RECOMMENDATION** Payroll reports and assistance cards regarding “Ama de Llaves” should be evaluated and reviewed by Program’s personnel before making any reimbursement of funds to the Municipality. The Municipality should adhere to annual Program’s budget authorized by the Lead Agency (OCAM).

**QUESTIONED COSTS** Questioned costs were not determined since amount paid in excess could not be calculated.

**MANAGEMENT RESPONSE  
AND CORRECTIVE ACTION PLAN** The Human Resources Department Director was informed about the Condition in order to request him the appropriate adjustments to the payroll system. Also, the Program Accountant was instructed to reimburse funds based on payrolls reports only.

Implementation Date: April 30, 2009

Responsible Person: Mrs. Nancy E. Rivera  
Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-04
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	COMPLIANCE
NONCOMPLIANCE	CASH MANAGEMENT
TOPIC SENTENCE	Non-Compliance with Cash Management Requirements
CONDITIONS	<p>Municipality's Community Development Block Grant / Small Cities Program (CDBG) do not complied with cash management requirements.</p> <p>During the fiscal year 2007-2008, the Municipality received approximately \$407,000 from CDBG. In order to determine compliance with the applicable cash management requirements, we selected for testing transfers of funds received during the fiscal year amounting \$402,000 (99%). The time elapsed between the receipt and the payment of such funds was from four to nine days. In addition, as June 30, 2008 the bank account balance counts with \$ 12,537.</p>
CRITERIA	As stated in 24 CFR 85.20(b)(7); 85.21(c) and 31 CFR 205.33, Subpart B, grantees must minimize the time between the drawdown of Federal funds from the Federal government and their disbursement for Federal program purposes. Also, 24 CFR 85.20(b)(3) establishes that effective control and accountability must be maintained for all grant cash and other assets.
CAUSE	The main cause for this condition was that, in occasions, once funds have been received they are being used to pay other obligations instead of the ones for which funds were requested. At the same time, this cause that obligations for which funds were previously requested have to be pay with funds requested later.
EFFECT	If the recipient fails to expend those Federal assistance funds within a reasonable period, or fails to establish procedures to minimize the time between the transfer and payout of funds, the Municipality could be subject to penalties from the State CDBG Program or the Federal Government and be adversely affected in the benefits they are entitled to receive in the future.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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FINDING	2008-04
RECOMMENDATION	The Program should implement adequate internal control procedures which allow the promptly use of federal funds received and ascertain that funds, once received, are used to pay those obligation for which they were requested.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Now, the time elapsed between the receipt and the disbursement of CDBG program funds is from four to nine days, but we will improve such lap of time in order to disburse funds in the next three to five days after receipt of funds.  Implementation Date: June 30, 2009  Responsible Person: Mrs. Nancy E. Rivera Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-05
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	COMPLIANCE
NONCOMPLIANCE	PROCUREMENT
TOPIC SENTENCE	Lack of adequate procurement procedures
CONDITIONS	<p>In testing compliance with the procurement requirement, we examined the processes carried out to procure goods and services which were paid during the fiscal year 2007-2008. In relation to such examination we determined the following deficiencies:</p> <ul style="list-style-type: none"><li>- Projects architecture design and supervision services amounting \$59,064 were contracted without obtaining at least three quotations or celebrating an adequate procurement process.</li><li>- As required by the Municipalities Law, we noted that in two out of three auctions files examined (66%), offers were received from companies or contractors which were not included on the Municipality's bidders register ( "Registro de Licitadores" ).</li></ul>
CRITERIA	<p>24 CFR 85.36 (c)(1)(4) state that all procurement transactions will be conducted in a manner providing full and open competition consistent with the standards of Sec. 85.36. Grantee and subgrantees will ensure that all prequalified lists of persons, firms, or products which are used in acquiring goods and services are current and include enough qualified sources to ensure maximum open and free competition.</p> <p>Chapter VIII, Part III, Section 1 of the Basic Standards for the Municipalities of Puerto Rico establishes that public bids will be announced by the municipalities each time procure goods or constructions works which exceed \$40,000 and \$100,000 dollars, respectively. On the other hand, Section 3(12) establishes that the invitation to an auction will be sent by mail to the persons or companies' representatives who appear in the bidders register.</p>
CAUSE	These conditions were caused due to the lack of adequate controls over the bidding process and the registering of bidders.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-05
EFFECT	Not carrying out the required procurement processes does not allow the Municipality to evaluate among different alternatives and select the one which provides the best benefits. The lack of documents and information as part of the bidding files does not allow understanding the rationale method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price. Furthermore the Municipality could be sanctioned by the State and Federal fiscal entities and adversely affected in the benefits they are entitled to receive in the future.
RECOMMENDATION	As part of the procurement process, the Municipality should assure that all bidders are included as part of the bidders register before they participates of an auction.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>Municipality of Peñuelas uses competitive proposal procedures for architectural/engineering professional services whereby competitors' qualifications are evaluated and the most qualified competitor is selected, subject to negotiation of fair and reasonable compensation. Each year, we request proposals for architectural/engineering professional services through a publication in general circulation newspapers in the Commonwealth of Puerto Rico.</p> <p>To correct the condition reported by the external auditors, we are going to evaluate and modify our method of conducting technical evaluations of the proposals received and for selecting awardees in order to assure that each stage of the process has documented in sufficient detail to assure that each record reflect the significant history of the procurement.</p> <p>Implementation Date: June 30, 2009</p> <p>Responsible Person: Mrs. Nancy E. Rivera Federal Programs Department Director</p>

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-06
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	COMPLIANCE
NONCOMPLIANCE	PROCUREMENT, SUSPENSION AND DEBARTMENT
TOPIC SENTENCE	Lack of required contracts provisions
CONDITIONS	As part of the evaluation of contracts granted to individuals and private entities from which the Municipality procured goods and services, we selected three contracts. Our test revealed that one out of three (33%) contracts examined does not contain a provision regarding legal remedies in instances where contractors violates or breach contract terms; retention of all required records for three years after grantees or subgrantees make final payments and all other pending matters are closed; access by the grantee and others to any books, documents, papers and records; and compliance with all applicable standards or requirements issued under the Environmental Protection Agency regulations.
CRITERIA	As stated in 24 CFR 85.36(i)(3)(4)(11) a grantee's and subgrantee's contracts must contain, among others, such provisions.
CAUSE	The Municipality has not ensured that all contracts granted counts with the required provisions due to the lack of understanding of the applicable Federal regulation.
EFFECT	Contracts failure to contain all required federal provisions could expose the Municipality of being liable for contractors non compliance with applicable federal laws and regulations contained within the required provisions.
RECOMMENDATION	The Municipality should verify and amend their contracts in order to include all required provisions as required by Federal regulations.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	To correct the condition reported by the external auditors, we are going to revise contract clauses in order to include all of contract provisions reported in the condition.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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Implementation Date: June 30, 2009

Responsible Person: Mrs. Nancy E. Rivera  
Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-07
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	COMPLIANCE
NONCOMPLIANCE	PROCUREMENT, SUSPENSION AND DEBARMENT
TOPIC SENTENCE	Non compliance over suspension and debarments
CONDITIONS	In testing procurement, suspension and debarments, we were not able to find evidence indicating that the Municipality performs procedures to assure that the individuals and entities which are granted with contracts are not suspended or debarred from participation if federal programs.
CRITERIA	As stated in 24 CFR 85.35 grantee and subgrantee must not make any award or permit any award (subgrant or contract) at any tier to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in Federal assistance programs under Executive Order 12549, "Debarment and Suspension".
CAUSE	The Municipality has no policies and procedures for the use of the List of Parties Excluded from federal procurement or non-procurement programs to assure that they do not award assistance to listed parties.
EFFECT	As a result of this deficiency, the Municipality could have procured goods or services from organizations and individuals that are suspended or debarred which could result in cost disallowances by the federal awarding agency.
RECOMMENDATION	The Municipality should amend their procurement procedures and include a step to verify whether or not the individual or entity is on the list of parties excluded from federal participation in procurement and nonprocurement programs. The Municipality should also require the entities or individuals to submit a certification stating that they are not suspended or debarred.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We will improve our procurement procedures including a step to verify through the electronic version available on the Internet ( <a href="http://epls.arnet.gov">http://epls.arnet.gov</a> ) whether or not the individual or entity is on the list of parties excluded from federal participation in procurement and non-procurement programs.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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Implementation Date: June 30, 2009

Responsible Person: Mrs. Nancy E. Rivera  
Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING** 2008-08

**FEDERAL PROGRAM** COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS

**CATEGORY** COMPLIANCE

**NONCOMPLIANCE** REPORTING

**TOPIC SENTENCE** Non compliance with reporting requirements

**CONDITIONS** Amounts reported during the fiscal year to the Lead Agency were incorrect. Reported amounts as of June 30, 2008 could not be traced to any accounting record or financial reports since they were not maintained. For such reason, in order to determine Programs' encumbrances and expenditures during the fiscal year, payment vouchers and obligations were individually examined. Based on such evaluation we noted that the amounts reported to the Lead Agency (OCAM) were under(over)stated as follows:

Activity per Program Year	Expenditures		Differences
	Per Quarterly Reports	Per Audit	
01-FD-008	\$ 75,559.08	\$ 395,701.81	\$ 320,142.73
03-FC-002	289,149.91	299,995.08	10,845.17
04-FC-003	26,263.13	41,113.79	14,850.66
05-FC-004	-	41,849.36	41,849.36
ADM-FD-2005	13,821.60	3,000.00	-10,821.60
05-AB-001	-	34,385.26	34,385.26
ADM-FC-2006	24,736.74	31,736.74	7,000.00
06-FC-001	-	21,444.00	21,444.00
ADM-AB-2006	39,753.13	42,753.13	3,000.00
06-AB-001	-	11,799.62	11,799.62
ADM-FC-2007	463.31	5,463.31	5,000.00
ADM-AB-2007	16,662.78	31,603.33	14,940.55

**CRITERIA** As specified in 24 CFR 85.20(b)(1), accurate, current, and complete disclosure of the financial results of financially asisted activities must be made in accordance with the financial reporting requirements of the grant.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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FINDING	2008-08
CAUSE	Lack of adequate accounting records and fiscal control.
EFFECT	The continuance occurrence of this situation inhibits the Lead Agency (OCAM) and other Federal award agencies from monitoring the programs financial performance. In addition, the Program could be sanctioned by the federal awarding agency due to the inaccurate filing of financial reports.
RECOMMENDATION	The Municipality should perform timely reconciliation and cutoff procedures between numbers kept at the federal programs and numbers recorded in the general ledger in order to provide reasonable assurance that reports of federal awards submitted to the federal awarding agency include all activity of the reporting period, are supported by underlying accounting or performance records, and are fairly presented in accordance with program requirements.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>The Program Accountant (recently engaged) is examining all of fiscal transactions since year 2001 to date in order to reconcile accounting records with reports submitted to the Lead Agency.</p> <p>Implementation Date: June 30, 2009</p> <p>Responsible Person: Mrs. Nancy E. Rivera Federal Programs Department Director</p>

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-09
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	INTERNAL CONTROLS
NONCOMPLIANCE	REPORTING
TOPIC SENTENCE	Inadequate fiscal control and lack of accounting records
CONDITIONS	<p>The Community Development Block Grants/Small Cities Program (the Program) does not maintain an adequate fiscal control and accounting records over the management, use and registering of funds granted by the Lead Agency (OCAM). Among the deficiencies founds were the following:</p> <ul style="list-style-type: none"><li>- The Program does not count with accounting records. Financial and accounting transactions are not being registered.</li><li>- The Program does not has a general ledger or any other related subsidiary ledger. For such reason, during the fiscal year 2007-2008 financial transactions were not registered neither reconciled, at least, on a monthly basis.</li><li>- The lack of accounting records does not provide for the preparation of an annual financial statements and monthly reports.</li><li>- The financial information provided does not allowed us to determine the amount of funds that were expended, encumbered or unobligated at the end of the fiscal year.</li><li>- Due to the lack of accounting records, we could not determine how administration costs were expended.</li><li>- The procedures followed by the Program to request funds from the Lead Agency (OCAM) are ineffective. As of June 30, 2008, total Program's administrative payroll costs incurred during the fiscal year had not been requested.</li></ul>

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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FINDING	2008-09
CRITERIA	<ul style="list-style-type: none"><li>- There are no internal controls neither records to account for the inter fund receivable and payables balances. Monthly Program's expenditures financed by the Municipality's general fund are not being register, monitored nor accounted for by the Program's accountant. In addition, inter fund transactions regarding the reimbursement of money between funds were not supported by an analysis.</li><li>- The Program does not count with adequate files or records regarding projects, housing rehabilitation, public service and administrative matters. Program's related documents were not properly safeguarded.</li><li>- Payments vouchers regarding payroll expenditures were not supported by payroll documents. In addition, payroll payments were made without reconciling such expenditures against the related payroll reports.</li><li>- Due to the lack of accounting records and adequate files we could not determined Program's complies with earmarking requirements.</li><li>- A budgetary control is not maintained.</li></ul> <p>Provision 17(6), (11), (14) and (16) of the Delegation of Funds Contracts subscribed with the Lead Agency (ACUDEN) require that the Program will maintain accounting subsidiaries, financial and accounting records, supporting documents, among others, that provide for the proper accountability, implementation of internal controls and monitoring from the Lead Agency and federal authorities. The Program will adopt written administrative and accounting procedures that provide for the trustworthiness of the financial information, and must maintain an adequate fiscal control that provide for the preparation of monthly and annual financial reports, budget control and bank account reconciliations. In addition, a file system and documents control should be maintain to guarantee documents security and conservation.</p> <p>45 CFR 98.67(c) establishes that fiscal control and accounting procedures shall be sufficient to permit: (1) preparation of reports; and (2) the tracing of funds to a level of expenditure adequate to establish that such funds have not been used in violation of the provisions of this part.</p>

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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FINDING	2008-09
CAUSE	<p>As stated in 45 CFR 92.20(a) Fiscal control and accounting procedures of the State, as well as its subgrantees, must be sufficient to (1) permit preparation of reports required by this part and the statutes authorizing the grant, and (2) permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restrictions and prohibitions of applicable statutes; (b) The financial management systems of other grantees and subgrantees must meet the following standards: (1) Accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant; (2) grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially-assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income; (3) Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes; (4) Actual expenditures or outlays must be compared with budgeted amounts for each grant or subgrant.</p>
EFFECT	<p>Program's accounting has been in hand of several accountants among the last fiscal years, what it has not allowed to giving continuity to the recording of accounting and financial transactions. In addition, the Municipality's and Program's management have not established the procedures and adequate internal controls to ensure the adequate recording, safeguarding and custody of all related financial information.</p>
RECOMMENDATION	<p>These conditions inhibit the Municipality from having current accurate and reliable financial reports and information necessary for management to take efficient and effective actions, including corrective actions plans. On the other hand, the awarding agency inhibits from monitoring the programs financial performance. Also, Municipality's failure to have accurate and complete accounting records could result in the qualification of the general purposes financial statements audit opinion.</p>
RECOMMENDATION	<p>The Municipality should establish a plan and implement the corresponding internal controls to ensure that all Program's transactions and activities are properly recorded and fairly presented in accordance with program requirements and that all financial transactions' supporting documents are properly safeguarded. In addition, should establish and maintain a subsidiary ledger to accurately account for inter fund transactions.</p>

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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FINDING 2008-09

QUESTIONED COSTS None

MANAGEMENT RESPONSE  
AND CORRECTIVE ACTION PLAN

The Program Accountant (recently engaged) is examining all of fiscal transactions since year 2001 to date in order to prepare a new set of accounting records.

Implementation Date: June 30, 2009

Responsible Person: Mrs. Nancy E. Rivera  
Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-10
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANT/SMALL CITIES (CDBG) (CFDA NO. 14.228) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE-OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS
CATEGORY	COMPLIANCE
NONCOMPLIANCE	SPECIAL TEST
TOPIC SENTENCE	Disbursement of funds before the request for release of funds
CONDITIONS	During the fiscal year 2007-2008, the Program encumbered and disbursed funds amounting \$46,180 before the related request of release of funds (RROF) were authorized for disbursements by the Lead Agency (OCAM). Funds were encumbered or paid five to eight months before the approval of the RROF.
CRITERIA	As stated in 24 CFR 58.22 neither a recipient nor any participant in the development process, including public or private nonprofit or for-profit entities, or any of their contractors, may commit HUD assistance under a program listed in 58.1(b) on an activity or project until HUD or the state has approved the recipient's RROF and the related certification from the responsible entity. In addition, until the RROF and the related certification have been approved, neither a recipient nor any participant in the development process may commit non-HUD funds on or undertake an activity or project under a program listed in 58.1(b) if the activity or project would have an adverse environmental impact or limit the choice of reasonable alternatives.
CAUSE	The Program incurred in such costs without receiving from the Lead Agency (OCAM) the adequate release of funds.
EFFECT	The Program could be sanctioned by the Lead Agency (OCAM) or any other federal awarding agency.
RECOMMENDATION	No funds should be encumbered or expended on an activity or project until the Lead Agency (OCAM) has approved the recipient's RROF.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	The Program accountant was instructed to not encumber or expend funds until the Lead Agency (OCAM) has approved the RROF.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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Implementation Date: June 30, 2009

Responsible Person: Mrs. Nancy E. Rivera  
Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-11
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS (CFDA NO. 14.871) DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
CATEGORY	COMPLIANCE
NONCOMPLIANCE	CASH MANAGEMENT
TOPIC SENTENCE	Non Compliance with cash management requirement
CONDITIONS	<p>Section 8 Housing Choice Voucher Program does not have adequate controls over the timing of disbursements once federal funds are received.</p> <p>During the fiscal year 2007 - 2008, the Municipality received \$844,465 from Section 8 Housing Choice Vouchers grant funds. In order to determine compliance with the applicable cash management requirements, we selected for testing four out of twelve transfers of funds received from the Federal during the fiscal year amounting \$232,548 (30%).</p> <p>The time elapsed between the receipt and the disbursement of such funds was from seven to ten days. We also noted that as of June 30, 2008, the Program maintained an account bank balance of approximately \$640,000.</p>
CRITERIA	As stated in 24 CFR 85.21(c) and 31 CFR 205.33, Subpart B, grantees must minimize the time between the drawdown of Federal funds from the Federal government and their disbursement for Federal program purposes.
CAUSE	Monthly deposits transferred by HUD are supported by an annual contribution contract based on an estimated number of occupied units and annual payments to owners. Due to the non identification of available dwelling units within the Municipality, the Program counts with a number of vouchers much higher than the amount of dwelling units available for rent. Such situation causes that, even when the Program counts with the necessary funds to provide housing assistance, these could not be expended due to the lack of units to be rented.
EFFECT	If the recipient fails to expend those Federal assistance funds within a reasonable period, or fails to establish procedures to minimize the time between the transfer and payout of funds, the Municipality could be adversely affected in the benefits they are entitled to receive in the future.

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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FINDING	2008-11
RECOMMENDATION	The Program should implement adequate internal control procedures which allow the promptly use of federal funds received. This could be attained through the identification of new participants and dwelling units ready for occupancy. Administrative funds should be budgeted, distributed and managed in a manner that provide for the promptly used of funds.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Actually, the time elapsed between the receipt and the disbursement of Section 8 program funds is from seven to ten days, but we will improve such lap of time in order to disburse funds in the next three to five days after receipt of funds. Also, the excessive Housing Assistance Payment (HAP) fund balance has been recaptured by HUD through the reduction of the monthly HAP funds transfers to the Municipality.  Implementation Date: June 30, 2009  Responsible Person: Mrs. Nancy E. Rivera Federal Programs Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-12
FEDERAL PROGRAM	HEAD START (CFDA NO. 93.600) DEPARTMENT OF HEALTH AND HUMAN SERVICES
CATEGORY	COMPLIANCE
NONCOMPLIANCE	Allowable costs / Cost principles
TOPIC SENTENCE	Allowable costs / Cost principles requirements
CONDITION	During the fiscal year 2003-2004, the program made a lease contract with the Puerto Rico Industrial Development Company (PRIDCO) to rent a local that will be the new administrative office of Head Start Program. The lease amount is of \$4,236 by month, for the first five (5) years. As of June 30, 2008, the program had paid the amount of \$12,708 and still has not yet moved to the new facilities.
CRITERIA	OMB Circular A-87, Attachment C, states that to be allowable under Federal awards, costs must meet the some general criteria, including the following: (a) be necessary and reasonable for proper and efficient performance and administration of Federal awards.
CAUSE	The Agency did not obtain the approval of funds in the "Program Improvement" proposal for the fiscal year 2002-2003 for the reason that the Administration of Children's and Families of the Department of Health and Human Services, Region II New York, the program's grantor, did not assigned funds for that activity in the Region.
EFFECT	The Municipality is not in compliance with OMB Circular A-87.
RECOMMENDATION	We recommend to the Municipality's management to request external funds or to assign local funds to make corresponding improvements to the new facilities, in order to relocate the administrative office of the Head Start Program.
QUESTIONED COSTS	\$12,708
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	The Municipality issued a special obligation bond to provide funds (non-federal funds) for the acquisition (\$600,000) and renovation (\$2,000,000) of the building leased to Puerto Rico Industrial Development Company (PRIDCO). We are in the process to continue the negotiations with the new PRIDCO administrators in order to acquire and renovate such facilities as planned.

Implementation Date: June 30, 2009

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

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Responsible Person:

Mrs. Wanda B. Jaime  
Head Start Program Department Director

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	2008-13
FEDERAL PROGRAM	HEAD START (CFDA NO. 93.600) DEPARTMENT OF HEALTH AND HUMAN SERVICES
CATEGORY	COMPLIANCE
NONCOMPLIANCE	Reporting
TOPIC SENTENCE	Reporting
CONDITION	Trial Balance has not been filed with the Lead State Agency on date required.
CRITERIA	Contract signed between the Lead State Agency and the Municipality requires in its clause ninth that the Municipality shall submit a Trial Balance at the closing of operations no later than the twenty days after the closing date.
CAUSE	Lack of proper supervision over the information requirements on contract with Lead State Agency was the cause of this condition.
EFFECT	The Municipality did not fully comply with the reporting requirements listed on contract with Lead State Agency.
RECOMMENDATION	We recommend to the Municipality's management to follow up on all reporting requirements listed on contract with Lead State Agency.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	The Program Accountant was instructed to file on time all reports required by the Lead State Agency.  Implementation Date: March 31, 2009  Responsible Person: Mrs. Wanda B. Jaime Head Start Program Department Director

END OF SCHEDULE

MUNICIPALITY OF PEÑUELAS, PUERTO RICO

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SCHEDULE OF PRIOR AUDIT'S FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2008

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(1) Audit Findings that have been Fully Corrected:

<b>Finding Number</b>	<b>CFDA</b>	<b>Questioned Cost</b>	<b>Comments</b>
07-05 Property & Equipment	14.228	None	Fully Corrected

(2) Audit Findings not corrected or Partially Corrected:

<b>Finding Number</b>	<b>CFDA</b>	<b>Questioned Cost</b>	<b>Comments</b>
07-02 Allowable Cost	93.600	\$50,835	Situation still prevails
07-03 Cash Management	14.228	None	Situation still prevails
07-04 Cash Management	14.871	None	Situation still prevails
07-06 Reporting	14.228	None	Situation still prevails
06-02 Real Property	93.600	\$50,835	Situation still prevails
05-III-04 Cash Management	14.871	None	Situation still prevails
05-III-07 Reporting	14.228	None	Situation still prevails
05-III-08 Davis Bacon Act	14.228	None	Situation still prevails
05-III-09 Property & Equipment	14.228	None	Situation still prevails
05-III-11 Real Property	93.600	\$50,835	Situation still prevails

(3) Corrective action taken is significantly different from corrective action previously reported:

NONE

(4) Audit findings is no longer valid:

NONE

END OF SCHEDULE

FINANCIAL DATA SCHEDULE  
REQUIRED BY  
U.S. DEPARTMENT OF HOUSING AND DEVELOPMENT