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AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL
AREA DE ARCHIVO DIGITAL

MUNICIPIO DE PONCE
AUDITORIA 2001-02
30 DE JUNIO DE 2002

Ortiz/Rivera 9646

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE**

**REPORTS ON COMPLIANCE AND INTERNAL CONTROL IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS
AND THE REQUIREMENTS OF OMB CIRCULAR A-133 AND
THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2002**

ORTIZ, RODRIGUEZ, RIVERA & CO.

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PART I

INDEPENDENT AUDITORS' REPORT

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FOR THE YEAR ENDED JUNE 30, 2002**

TABLE OF CONTENTS

	PAGE
PART I INDEPENDENT AUDITORS' REPORT ON:	
Compliance and on Internal Control over Financial Reporting Based on an Audit of the Financial Statements Performed in Accordance with Government Auditing Standards	2
Compliance and Internal Control over Compliance Applicable to Each Major Federal Award Program and on the Schedule of Expenditures of Federal Awards	4
PART II SCHEDULE OF FINDINGS AND QUESTIONED COSTS	7
PART III FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON THE AUDIT OF THE BASIC FINANCIAL STATEMENTS	10
Budgeting	17
Accounting and Finance Department	22
Purchases, Payables and Payments	30
Municipal License Tax – Revenue and Deferred Revenue	36
Payroll and Personnel	37

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TABLE OF CONTENTS

	PAGE
PART IV FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS	40
Finding Related to Federal Programs that have a Separate Accounting Department and Administrative Unit	41
<u>Department of Housing and Urban Development Programs</u>	
Community Development Block Grant	43
Section 8 Housing Choice Voucher	57
Section 8 Project-Based Cluster	65
HUD Disaster Recovery Initiative	67
<u>Department of Labor Programs</u>	
Workforce Investment Act Cluster	76
<u>Health and Human Services Administration Programs</u>	
Administration for Children, Youth and Families - Head Start Program	79
PART V PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS	89
PART VI SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS	107
Notes to Schedule of Expenditures of Federal Awards	109
PART VII CORRECTIVE ACTION PLANS ON CURRENT YEAR FINDINGS	111

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

Honorable Mayor and Members of the Municipal Legislature
Municipality of Ponce
Ponce, Puerto Rico

We have audited the basic financial statements of the Municipality of Ponce, Puerto Rico (the "Municipality") as of and for the year ended June 30, 2002 and have issued our report thereon dated October 25, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, applicable to the Municipality for only those matters relating to compliance of the funds and governmental activities of the Municipality included within the scope of our audit as described in our report referred to above on the basic financial statements, 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 that are required to be reported under *Government Auditing Standards*, which are described in the accompanying Schedule of Findings and Questioned Costs as items 02-01 through 02-10. Our testing of compliance did not extend to tests of compliance with laws, regulations, contracts and grants for the discretely presented component units whose financial statements were audited by other auditors.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the Municipality's internal control over financial reporting, applicable only to the internal control over financial reporting relating to the primary government of the Municipality included within the scope of our audit as described in our report referred to above on the basic financial statements, in order to determine our auditing

procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Accordingly, our consideration did not extend to the internal control over financial reporting relating to the discretely presented component units whose financial statements were audited by other auditors. However, we noted certain matters involving the internal control over financial reporting of the primary government and its operations that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Municipality's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs, included in Part II.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable condition and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 02-01, 02-03, 02-04, 02-05, 02-08, and 02-10 to be material weaknesses.

This report is intended solely for the information and use of the Municipal Legislature, management, 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.

Ortiz, Rodriguez, Rivera & Co.

October 25, 2002
San Juan, Puerto Rico

The stamp 1847868 was affixed
to the original of this report.



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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL OVER
COMPLIANCE APPLICABLE TO EACH MAJOR FEDERAL AWARD PROGRAM AND ON
THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**

Honorable Mayor and Members of the Municipal Legislature
Municipality of Ponce
Ponce, Puerto Rico

Compliance

We have audited the compliance of the Municipality of Ponce, 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 year ended June 30, 2002. 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 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 other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Municipality's compliance with those requirements.

As described in the table below, and in the accompanying Schedule of Findings and Questioned Costs, the Municipality did not comply with the requirements regarding activities allowed or unallowed; allowable costs/cost principles; cash management; eligibility; matching, level of effort and earmarking; period of availability of Federal funds; program income; reporting; subrecipient monitoring, and applicable special tests and provisions that are applicable to its Community Development Block Grant, HUD Disaster Recovery Initiative, Section 8 Housing Choice Vouchers, Section 8 Project-Based Cluster, Public Safety Partnership and Community Policing Grant, Welfare-to-Work, Workforce Investment Act

Cluster, Public Assistance Grants, Administration for Children, Youth and Families (“Head Start”) and HIV Cluster - HIV Emergency Relief Project and Formula Grants (“Ryan White”). Compliance with such requirements is necessary, in our opinion, for the Municipality, to comply with requirements applicable to these programs.

<u>Requirements</u>	<u>Items Number - SA -</u>	<u>Programs</u>
Activities allowed or unallowed	SA-02-02, 02-9, 02-21	Community Development Block Grant, Section 8 Housing Choice Voucher
Allowable costs/cost principles	SA-02-02, 02-9, 02-21	Community Development Block Grant, Section 8 Housing Choice Voucher
Cash management	SA-02-01, 02-04, 02-08, 02-11, 02-15, 02-18, 02-24	Community Development Block Grant, Section 8 Housing Choice Voucher, HUD Disaster Recovery Initiative, Workforce Investment Act, Head Start, and Welfare to Work
Eligibility	SA-02-10	Section 8 Housing Choice Voucher
Matching, level of effort and earmarking	SA-02-07, SA-02-07, 02-14	Community Development Block Grant, and HUD Disaster Recovery Initiative
Period of availability of Federal Funds	SA-02-12	HUD Disaster Recovery Initiative
Program - income	SA-02-06, 02-23	Community Development Block Grant , Loan Guarantee
Reporting	SA-02-01, 02-03, 02-13, 02-16, 02-25	Community Development Block Grant, HUD Disaster Recovery Initiative, Workforce Investment Act, Head Start, and Ryan White
Subrecipient monitoring	SA-02-26	Ryan White
Special tests and provisions	SA-02-17, 02-19	Head Start
Noncompliance with pledge requirement	SA-02-22	Loan Guarantee Assistance

In our opinion, except for the noncompliance described in the preceding paragraph and accompanying table, 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 year ended June 30, 2002. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items SA-02-01 and SA-02-26.

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, contract, and grants applicable to federal programs. In planning and performing our audit, we considered the Municipality’s internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over

compliance that, in our judgment, could adversely affect the Municipality's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items SA-02-01 through 02-26.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items SA-02-01, 02-02, 02-04, 02-05, 02-08, 02-09 through 02-19, to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of the Municipality as of and for the year ended June 30, 2002, and have issued our report thereon dated October 25, 2002. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for the purpose of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. This schedule is the responsibility of management of the Municipality. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects when considered in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Municipal Legislature, management, 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.

Ortiz, Rodriguez, Rivera & Co.

October 25, 2002
San Juan, Puerto Rico

The stamp 1847869 was affixed
to the original of this report.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE

PART II

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

- 7 -

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MUNICIPALITY OF PONCE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2002

1. Summary of Auditors' Results

We have audited the basic financial statements of the Municipality of Ponce, Puerto Rico as of and for the year ended June 30, 2002, and have issued our report thereon dated October 25, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the requirements of the *U.S. Office of Management and Budget (OMB) Circular A-133*. The results of our audit are as follows:

Financial Statements:

- Type of auditor's report issued on the basic financial statements: Unqualified Opinion
- Reportable conditions in internal control over financial reporting were identified, some of which are considered to be material weaknesses.
- Instances of noncompliance considered material to the financial statements were disclosed by the audit.

Federal Awards:

- Reportable conditions in internal control over compliance with requirements applicable to major federal award programs were identified, some of which are considered to be material weaknesses.
- The independent auditor's report on compliance with requirements applicable to major federal award programs expressed a qualified opinion.
- The audit disclosed findings required to be reported by OMB Circular A-133.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2002

- Major Programs:

<u>Funding Source</u>	<u>Program</u>	<u>CFDA No.</u>
U.S. Department of Housing	Community Development Block Grant	14.218
U.S. Department of Housing	HUD Disaster Recovery Initiative	14.218
U.S. Department of Housing	Section 8 Housing Choice Voucher	14.871
U.S. Department of Housing	Section 8 – Project-Based Cluster:	
	Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation I	14.856
	Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation II	14.856
U.S. Department of Labor	Workforce Investment Act Cluster:	
	WIA - Adult Program	17.258
	WIA – Youth Activities	17.259
	WIA – Dislocated Workers	17.260
U.S. Department of Health and Human Services	Administration for Children, Youth and Families (“Head Start”)	93.600

- A threshold of \$1,275,074 was used to distinguish between Type A and Type B programs as those terms are defined in OMB Circular A-133.
- The Municipality did not qualify as a low-risk auditee as that term is defined in OMB Circular A-133.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2002

1. Introduction

The findings and recommendations as defined in Part III which are summarized in the schedule below, have been reviewed with representatives of the Municipality. In the title of each finding is a parenthetical disclosure indicating the first year that the finding was reported, and the finding number from the previous year audit report. The corrective action plans and responses to the findings and recommendations have been provided by the Municipality's representatives and reflect plans and responses as of March 21, 2003 and are included in Part VII. These responses and corrective action plans were delivered to us after completion of our field work and, accordingly, our procedures with respect to such corrective action plans consisted of reading the Municipality's response and including them within the body of the findings. Although the responses may indicate that the supporting documentation is available for examination, the finding is not eliminated because such evidence was found after we concluded the fieldwork.

The findings and recommendations often refer to the provisions of various authoritative documents, laws and regulations. To avoid repetition, following are the authoritative documents with their respective titles and purposes, quoted in the findings and recommendations:

1. **"Single Audit Act Amendments of 1996"** - The Single Audit Act Amendments of 1996, Public Law 104-156, enacted on July 5, 1996, by the Senate and House of Representatives of the United States of America in Congress. The Act was established to a) promote sound financial management, including effective internal controls, with respect to Federal awards administered by non-Federal entities; b) establish uniform requirements for audits of Federal awards administered by non-Federal entities; c) promote the efficient and effective use of audit resources; d) reduce burdens on State and local governments, Indian tribes, and nonprofit organizations; and e) ensure that Federal departments and agencies, to the maximum extent practicable, rely upon and use audit work done pursuant to chapter 75 of title 31, United States Code (as amended by this Act).
2. **"OMB Circular A-133"** - Circular Letter A-133 issued by the Executive Office of the President, Office of Management and Budget, titled "Audits of States, Local Governments, and Non-Profit Organizations" dated June 24, 1998. This Circular Letter establishes the audit requirements for States, Local governments and Non-Profit Organizations that receive Federal aid, and defines Federal responsibilities for implementing and monitoring those requirements. It sets forth standards for

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2002

obtaining consistency and uniformity among Federal agencies for the audit of States, local governments, and non-profit organizations expending Federal awards.

3. **"OMB Circular A-87"** - Circular Letter A-87 issued by the Executive Office of the President, Office of Management and Budget, titled "Cost Principles for State, Local and Tribal Governments," dated May 4, 1995. This Circular Letter establishes the principles for determining the allowable costs of programs administered by State, Local, and federally recognized Indian tribal governments under grants from and contracts with the Federal government.
4. **"OMB Circular A-102"** - Circular Letter A-102, (Revised), issued by the Executive Office of the President, Office of Management and Budget, titled "Grants and Cooperative Agreements with State and Local Governments," dated March 3, 1988. This Circular Letter establishes consistency and uniformity among Federal agencies in the management of grants and cooperative agreements with State, Local, and federally recognized Indian tribal governments.
5. **"CFR"** - This is the "Code of Federal Regulations" issued by the Federal Government. The CFR is a codification of the general and permanent rules published by the Federal Government. The Code is divided into 50 titles that represent broad areas subject to Federal regulation. Each title is divided into chapters that usually bear the name of the issuing agency, and is further subdivided into parts covering specific regulatory areas.
6. **"Common Rule"** - The Common Rule refers to the "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments" which establishes uniform administrative rules for Federal grants and cooperative agreements and subawards to State, local, and Indian Tribal governments.
7. **"Basic Standards"** - "Revised Regulation on Basic Standards for the Municipalities of Puerto Rico" approved by the Office of the Commissioner of Municipal Affairs. The Basic Standards were created under Article 19.011 of Law 81, enacted on August 30, 1991, "Autonomous Municipalities Law of the Commonwealth of Puerto Rico". It establishes the rules and operational standards applicable to the municipalities in relation to the accountability of funds, property and other financial and fiscal matters administered by the municipalities of Puerto Rico. Its main purpose is to allow for the efficient use and administration of the municipal operations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2002

8. **"Autonomous Municipalities Law of the Commonwealth of Puerto Rico"** - The "Autonomous Municipalities Law of the Commonwealth of Puerto Rico", Law 81 of August 30, 1991, as amended, was enacted to establish standard rules and regulations regarding the creation, organization, administration and functions of the municipal governments in Puerto Rico. It establishes the main guidelines and requirements that governs all the municipal functions and activities.

Questioned Costs:

The audit of compliance with laws and regulations, and the audit of the basic financial statements of the Municipality resulted in the identification of questioned costs totaling \$332,007 for the year ended June 30, 2002. For those instances where costs were questioned, the specific cost has been identified in the findings reported in the following pages. On pages 13 to 15 we have included those questioned costs in the summarized information in the table titled Schedule of Findings and Questioned Costs.

The Schedule of Findings and Questioned Costs presented in Part II, as listed in the table of contents, includes items arising from the Single Audit for the year ended June 30, 2002. Questioned costs noted in the reports of federal auditors and proposed, or pending sanctions arising from programmatic reviews by federal agencies, if any, were reviewed to determine the nature of the item and its current status. This information was considered during the development of the current year's audit procedures. The final resolution of the items arising from other audits and reviews, as well as disposition of the questioned costs included in Part II, "Schedule of Findings and Questioned Costs," as listed in the table of contents, rests with the federal grantor agencies.

Reportable Conditions:

The findings listed on pages 16 through 106 have been reported in accordance with the requirements of Government Auditing Standards, issued by the Comptroller General of the United States and the Statements on Auditing Standards 60 and 74, issued by the Auditing Standards Board of the American Institute of Certified Public Accountants. These standards require the communication of all reportable conditions regarding the entity's internal controls.

Reportable conditions are those matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operation of the internal control structure, which could adversely affect the organization's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements and in reports applicable to its federal

- 12 -

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2002

financial assistance programs. Such deficiencies may involve aspects of the internal control structure elements of (a) control environment; (b) the accounting system; or (c) control procedures.

2. Findings Related to the Financial Statements

<u>Reportable Condition/Noncompliance</u>	<u>Questioned Costs</u>	<u>Program and CFDA No.</u>
<u>Budgeting</u>		
02- 1 Operating deficit of general fund	N/A	N/A
02- 2 Estimates of expenditures not submitted	N/A	N/A
<u>Accounting and Finance Department</u>		
02- 3 Inadequate accounting practices and policies	N/A	N/A
02- 4 Inadequate accounting for interfund transactions	N/A	N/A
02- 5 Inactive and unnecessary funds and accounts are not closed	N/A	N/A
02- 6 Checks outstanding in excess of six months	N/A	Workforce Investment Act (17.258, 17.259, and 17.260), Head Start (93.600)
<u>Purchases, Payables and Payments</u>		
02- 7 Construction excise tax files not available	N/A	N/A
02- 8 Inadequate controls over vouchers for payments and related documents	N/A	N/A
<u>Municipal License Tax - Revenue and Deferred Revenue</u>		
02- 9 Lack of supporting documentation for municipal license taxes files	N/A	N/A
<u>Payroll and Personnel</u>		
02- 10 Incomplete documentation in employee files	N/A	N/A

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2002**

3. Findings and Questioned Costs for Federal Awards

<u>Reportable Condition/Noncompliance</u>		<u>Known Questioned Costs</u>	<u>Likely Questioned Costs</u>	<u>CFDA No.</u>
<u>Finding Related to Federal Programs That Have a Separate Accounting Department and Administrative Unit</u>				
SA 02- 1	Lack of reconciliation procedures	N/A	N/A	All Federal Programs
<u>Community Development Block Grant</u>				
SA 02- 2	Amounts due from general fund	N/A	N/A	14.218
SA 02- 3	Financial summary report is inaccurate	N/A	N/A	14.218
SA 02- 4	Inadequate cash management procedures	N/A	N/A	14.218
SA 02- 5	Unliquidated obligations of closed program years not credited to federal program	N/A	N/A	14.218
SA 02- 6	Failure to monitor program-income producing activities	N/A	\$ 10,000	14.218
SA 02- 7	Interest earned not remitted to federal grantor	9,156	N/A	14.218
<u>Section 8 Housing Choice Voucher</u>				
SA 02- 8	Inadequate cash management procedures	N/A	N/A	14.871
SA 02- 9	Amounts due from general fund	N/A	N/A	14.871
SA 02- 10	Inadequate documentation of participant files	N/A	N/A	14.871
<u>HUD Disaster Recovery Initiative</u>				
SA 02- 11	Inadequate cash management procedures	N/A	N/A	B-98MU-72-0003
SA 02- 12	Noncompliance with period of availability of federal funds	N/A	N/A	B-98MU-72-0003
SA 02- 13	Ineffective controls over preparation and submission of federal financial reports	N/A	N/A	B-98MU-72-0003
SA 02- 14	Noncompliance with earmarking requirements	N/A	N/A	B-98MU-72-0003
<u>Workforce Investment Act Cluster</u>				
SA 02- 15	Inadequate cash management procedures	N/A	N/A	17.258, 17.259 and 17.260

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2002**

3. Findings and Questioned Costs for Federal Awards...Continued

<u>Reportable Condition/Noncompliance</u>	<u>Known Questioned Costs</u>	<u>Likely Questioned Costs</u>	<u>CFDA No.</u>
<u>Administration for Children, Youth and Families</u>			
SA 02- 16 Ineffective controls over preparation and submission of federal financial reports	N/A	N/A	93.600
SA 02- 17 Failure to meet full enrollment level	322,851	N/A	93.600
SA 02- 18 Inadequate cash management procedures	N/A	N/A	93.600
SA 02- 19 Failure to meet the minimum required average daily attendance level	N/A	N/A	93.600
<u>Public Assistance Grants</u>			
SA 02- 20 Lack of formal accounting records to support federal financial reports	N/A	N/A	83.544
<u>Loan Guarantee Assistance</u>			
SA 02- 21 Amounts due from general fund	N/A	N/A	14.218
SA 02- 22 Noncompliance with pledge requirement	N/A	N/A	14.218
SA 02- 23 Failure to monitor program income producing act.	N/A	N/A	14.218
<u>Welfare to Work</u>			
SA 02- 24 Inadequate Cash Management Procedures	N/A	N/A	17.253
<u>HIV Cluster - HIV Emergency Relief Project and Formula Grants</u>			
SA 02- 25 Lack of formal accounting records to support federal financial reports	N/A	N/A	93.914 and 93.915
SA 02- 26 Ineffective monitoring procedures	<u>N/A</u>	<u>N/A</u>	93.914 and 93.915
Total Questioned Costs	<u>\$ 332,007</u>	<u>\$ 10,000</u>	

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PART III

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON THE AUDIT OF THE
BASIC FINANCIAL STATEMENTS**

-16 -

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

BUDGETING

Finding Number 02-01: Operating Deficit of General Fund (Prior Report Finding Number 01-01) (First Reported 1986):

Condition:

The Municipality's system of internal control relating to the Budgeting function does not adequately prevent operating management from incurring expenditures in excess of the level of funds appropriated and available. The Municipality closed its fiscal year ended June 30, 2002 with a deficiency in the general fund in the governmental funds financial statement of approximately \$20.1 million, and an operating deficiency of expenditures over revenues of approximately \$9.8 million.

Criteria:

Article 8.004 Section (b) of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico establishes that the Municipality cannot obligate or spend funds in excess of the appropriations for the ensuing fiscal year. In addition, according to Chapter IV, Section 17, of the Basic Standards, the responsibility of oversight to prevent deficits in any municipal fund rests with the Finance Director. Also, the Article 7.011, Section (a) of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico, establishes that: "If there is an operating deficit at the end of a fiscal year, the municipality is obligated to include in the next year budget the necessary and sufficient sources to respond for the credit of the prior fiscal year."

Cause:

This occurs because the budgeting system does not prevent the obligation of expenditures for which current resources will not be available.

Effect:

The continued occurrence of this situation could result in the eventual reduction or elimination of municipal services since future revenues will need to be used to pay for accumulated liabilities.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

BUDGETING

Finding Number 02-01: Operating Deficit of General Fund (Prior Report Finding Number 01-01) (First Reported 1986)...(Concluded):

Recommendation:

The Municipality should include in the next year budget the necessary resources to respond to the deficiency in general fund from prior and current fiscal years.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

BUDGETING

Finding Number 02-02: Estimates of Expenditures not Submitted (Prior Report Finding Number 01-03) (First Reported 1999):

Condition:

The Municipality's system of internal control over the preparation of the annual budget of the general fund is not effective. We noted that 4 out of 24 Municipal Departments, (16%), did not submit the estimates of expenditures for the preparation of the 2001-2002 operational budget of the general fund to the Budget Department. The departments in which this exception occurred were as follows:

<u>DEPARTMENT</u>	<u>APPROVED BUDGET</u>
Permit Office	\$ 1,349,368
Budget and Management	1,499,515
Industrial Economic Development	269,101
C.I.D.E.S.	118,550
	<u>\$ 3,236,534</u>

The approved budget for these departments represents 4% of the total budget of the general fund, which totaled approximately \$77.7 million.

Criteria:

Chapter II, Section 4(1) of the Basic Standards requires each of the Municipal Department Directors to prepare and submit to the Budget Department an estimate of expenditures for the year. This information should be used by the Budget Department to prepare the operational budget for the year.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

BUDGETING

Finding Number 02-02: Estimates of Expenditures not Submitted (Prior Report Finding Number 01-03) (First Reported 1999)...(Concluded):

Cause:

This condition results from the failure of the corresponding Department Directors to monitor compliance with the reporting requirements by ensuring the timely preparation and submission of expenditure estimates to the Budget Department. In addition, the Budget Department failed to follow-up and obtains the documents before the preparation and approval of the general fund's budget. Accordingly, the budgets for these departments were approved without being reviewed and analyzed by the Budget Department.

Effect:

The continued failure to obtain the estimate of expenditures may result in the approval of amounts either in excess of or less than those necessary to meet the actual needs of the corresponding departments. Furthermore, deviations from budget will be difficult to analyze since the original detail is not available for comparison with actual expenditures within the department.

Recommendation:

The Municipality should establish a reporting calendar that informs the Department Directors of the due dates of each financial report. The calendar will help to establish priorities by ensuring that management is aware of dates that expenditure estimates should be submitted to the Budget Department. Department Directors must ensure compliance with reporting deadlines. The Budget Director should not submit the budget for the approval of the Mayor and the Municipal Assembly whenever there are significant unsupported amounts included within the budget. The Mayor and Municipal Assembly should consider appropriate action to be taken against Departments that do not submit information. Such action could include budget reductions or other penalties to operations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

BUDGETING

FINDINGS NOT REPEATED FROM PRIOR AUDIT

- Finding Number 01-02: Expenditures Quarterly Reports not Submitted – During our audit we noted that the expenditure reports are submitted on a monthly basis.
- Finding Number 01-04: Lack of Supporting Documentation for Budgeted Revenue Account – Our audit procedures did not disclose that this deficiency was repeated during current year.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

ACCOUNTING AND FINANCE DEPARTMENT

Finding Number 02-03: Inadequate Accounting Practices and Policies (Prior Report Finding Number 01-05) (First Reported 1986):

Condition:

The accounting system only provides for the recording of revenues, expenditures, certain balance sheet accounts and a limited number of other transactions. Therefore, the basic financial statements must be prepared using financial information obtained from various departments and accounting records. The records are not integrated, and do not follow a double entry system (debits and credits). As a result the records required significant adjustment in order to present the financial position and results of operations of the Municipality in conformity with accounting principles generally accepted in the United States of America.

There were significant differences between the records kept at the accounting department and those for the federal programs. Financial reports for all fund types showing the financial position and results of operations following accounting principles generally accepted in the United States of America are only prepared at the time of the annual audit.

Criteria:

In summary, the current accounting system does not comply with the requirements established in Article 8.010, Sections (b) and (c) of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico. These sections provide the following:

Section (b) - Municipal accounting shall be kept by funds and in conformity with accounting principles generally accepted in the United States of America and the requirements established by the Governmental Accounting Standards Board. Also, it should be based on the pronouncements of the National Committee on Governmental Accounting and the book Governmental Accounting, Auditing and Financial Reporting. This publication should serve as the basis for designing the accounting practices and policies to allow for the preparation of the basic financial statements.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

ACCOUNTING AND FINANCE DEPARTMENT

Finding Number 02-03: Inadequate Accounting Practices and Policies (Prior Report Finding Number 01-05) (First Reported 1986)...(Concluded):

Section (c) - The accounting system should provide:

1. the complete results of the Municipal operations,
2. the proper and necessary financial information for the efficient administration of the Municipality,
3. effective controls and the accountability of all the funds, property and other municipal assets,
4. information necessary for the preparation of accurate financial reports, that could be used in the preparation of the municipal budget.

Cause:

The communication between the different municipal departments, federal programs, and the Office of Finances is not effective. This deficiency in communication also is reflected between the Office of Municipal License and the Office of Construction Excise Tax where does not exist a control that can track the payment of the contributor in both departments.

The Municipality does not maintain adequate records of outstanding long-term obligations. The practice is to rely upon the notification received from the Government Development Bank for Puerto Rico or the Federal government for the balance of its outstanding debt and the withholdings for its debt service.

Effect:

The continued failure to have an adequate accounting system prevents the Municipality from having current accurate and reliable financial reports and information necessary for management to take efficient and effective actions, including corrective actions when plans and objectives are not being met.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

ACCOUNTING AND FINANCE DEPARTMENT

Finding Number 02-03: Inadequate Accounting Practices and Policies (Prior Report Finding Number 01-05) (First Reported 1986)...(Concluded):

Recommendation:

The Municipality should adopt and implement a plan to convert its accounting system to an integrated system that would allow for the monthly closing of the ledger, as well as the preparation of year-end financial statements in accordance with accounting principles generally accepted in the United States of America. This plan should provide for:

- the implementation of a double entry accounting system, the integration of all subsidiary ledgers and the reconciliation with the records maintained for the federal funds,
- the preparation of periodic financial reports to be submitted to the Mayor, the Finance Director, the Municipal Assembly and all other interested entities,
- adequate training of all accounting personnel to improve the understanding of the system and to promote operational efficiency,
- the Municipality should implement monthly reconciliation of the transactions recorded in each of the programs with the transactions processed and recorded in the central accounting department. In addition, it should ensure that all federal financial reports are prepared based on the financial information once reconciled.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

ACCOUNTING AND FINANCE DEPARTMENT

Finding Number 02-04: Inadequate Accounting for Interfund Transactions (Prior Report Finding Number 01-06) (First Reported 1986):

Condition:

The Municipality has not established appropriate accounting policies for the recording of interfund transactions. Transfers among different funds are accounted for as "expenditures" in the fund making the transfer and as "revenues" in the receiving fund. There are no subsidiary accounts to accurately account for the interfund receivable and payable balances.

Criteria:

Article 8.010, Section (b) of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico establishes that the accounting system shall provide for the accounting procedures and records to be maintained in accordance with accounting principles generally accepted in the United States of America applicable to governmental entities.

Cause:

The Municipality determined the amounts to be presented in the basic financial statements after searching for transfer transactions in its accounting records; this process increases the risk that such transactions could be missed or incorrectly accounted for. No consideration is given to the nature of the transaction as a transfer or as an interfund loan. Accordingly, revenues, expenditures, and interfund receivables and payables were adjusted for financial reporting purposes to conform to the presentation in accordance with accounting principles generally accepted in the United States of America. As of June 30, 2002, the general fund owed \$2,619,579 to HUD, HUD owed \$16,463 to general fund, other funds owed \$326,114 to general fund, and general fund owed \$1,315 to Head Start.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

ACCOUNTING AND FINANCE DEPARTMENT

Finding Number 02-04: Inadequate Accounting for Interfund Transactions (Prior Report Finding Number 01-06) (First Reported 1986)...(Concluded):

Effect:

The lack of accounting records for interfund transactions may result in the use of one fund's resources to finance the activities of another fund, and the money not being reimbursed to the proper fund. Since most of the balance results from transfers to the general fund from federal financial assistance programs, they have been reported as questioned costs in previous years' Single Audit reports. Accordingly, there is the possibility that the Municipality may need to refund the balances of the amounts owed to the federal agencies, including the possibility of being assessed penalties and interest costs on such advances.

Recommendation:

The Municipality should establish and maintain a subsidiary ledger to accurately account for interfund transactions as provided by Article 8.010, Section (b) of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico. Furthermore, the Municipality should immediately refund amounts owed to the federal funds to prevent the assessment of interest and penalties on such funds.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

ACCOUNTING AND FINANCE DEPARTMENT

**Finding Number 02-05: Inactive and Unnecessary Fund and Account are Not Closed
(Prior Report Finding Number 01-07) (First Reported 1986):**

Condition:

The Municipality is maintaining funds and accounts that have been inactive for a long period. The Municipality's accounting records include accounts that have been inactive or did not have significant operations during the year 2001-02. The inactive accounts were the followings:

<u>Account Name</u>	<u>Bank Account Number</u>	<u>Balance</u>
Rental Loan	129-06264	\$ 84
Quality One Health	901-740129	7,883

Criteria:

Article 8.007 Section (b), of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico establishes that funds should be closed when the fund's objectives have been completed.

Cause:

This occurs because the Municipality has not analyzed and closed inactive funds as well as the related bank accounts when the funds' objectives have been achieved or are no longer relevant.

Effect:

The continued maintenance of these funds and accounts exposes the Municipality to the unauthorized use of funds from inactive accounts for activities not intended to be financed with these funds and to accounting errors as a result of inappropriate postings to the accounts.

Recommendation:

The Municipality should determine whether the intended objectives of these funds were met. The Municipality should close all funds that have complied with the requirements. Remaining balances in those funds should be transferred in accordance with local and federal regulations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

ACCOUNTING AND FINANCE DEPARTMENT

**Finding Number 02-06: Checks Outstanding in Excess of Six Months (Prior Report
Finding Number 01-08) (First Reported 1992):**

Condition:

The Municipality is not canceling outstanding checks, which have been outstanding for a period in excess of six months in the following accounts:

Name of Account	Bank Account Number	Number of Checks	Total Amount
Head Start	071-036911	4	\$ 1,467.11
WIA	071-076492	5	552.13

Criteria:

Chapter IV, Section (11) of the Basic Standards establishes that checks outstanding for more than one year should be cancelled and the amount included in the cash balance, furthermore the municipal checks are not valid six months after being issued.

Cause:

This is caused by the lack of a regular monthly review and follow up of bank reconciliation, specifically those with many outstanding checks, and the need to establish investigation procedures to determine the underlying reasons as to why these checks have not been presented for payment.

Effect:

This situation represents a possible understatement of cash and an overstatement of expenditures and, in the case of federal funds, could result in questioned and disallowed costs.

Recommendation:

The Municipality should evaluate the outstanding checks list on a monthly basis, and investigate checks that have not cleared the bank for an unreasonable period of time (i.e. three to six months), contact the payee and determine the underlying reasons as to why these have not been presented to the bank for payment.

- 28 -

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**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

FINDING NOT REPEATED FROM PRIOR AUDIT

- Finding Number 01-09: Banks Reconciliation not Prepared on a Timely Basis – Our audit procedures did not disclose that banks reconciliation were not prepared on a timely basis.
- Finding Number 01-10: Untimely Contract of External Auditors – Our audit was contracted timely.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

PURCHASES, PAYABLES AND PAYMENTS

Finding Number 02-07: Construction Excise Tax Files not Available:

Condition:

The Municipality could not provide us two files related to construction excise tax from a sample of 35 files.

Date of the receipt	Name	Official Receipt Number	Amount
8/6/2001	Branch Constructions S. E.	2207058	\$ 56,880
2/26/2002	Atlante Corp.	2218308	59,676
			<u>\$ 116,556</u>

Criteria:

Article 2.007 of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico establishes that the person responsible of the realization of the project should file to the Finance Department of the Municipality an Activity Declaration that describes the costs of the project to be realized. In addition, Chapter III, Section 5 of the Basic Standards establish that the Finance Director shall be responsible to safeguard and keep the documents and files available for examination of the Comptroller's Office of Puerto Rico and the Commissioner of Municipal Affairs.

Cause:

The Municipality's internal control procedures regarding the filing of documents are inadequate.

Effect:

The continued failure to maintain adequate documentation of construction excise tax files prevents the Municipality from having current accurate and reliable reports.

Recommendation:

The Municipality should ascertain that adequate source documentation of construction excise tax files exists to support any amounts reported in the general ledger.

- 30 -

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**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

PURCHASES, PAYABLES AND PAYMENTS

Finding Number 02-08: Inadequate Controls over Vouchers for Payment and Related Documents:

Condition:

The Municipality's system of internal control over purchasing and payments is not effectively ensuring the completeness of vouchers for payment and the related documentation. We select a sample of 63 vouchers of ordinary fund and 125 vouchers of other funds to be examined:

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

PURCHASES, PAYABLES AND PAYMENTS

Finding Number 02-08: Inadequate Controls over Vouchers for Payment and Related Documents:

Check Number	Voucher Number	Amount	Finding
51745	2004274	87,500.00	B
51751	2004279	87,500.00	B
52849	2006011	130,000.00	B
53854	2007519	247,138.07	B
54777	2008846	100,000.00	C
000246	02000246	117,309.60	D
000253	02000253	751,630.50	D
000267	02000267	398,309.40	D
002338	02002338	224,340.00	E
003048	02003048	720,974.10	B
004337	02004337	95,950.00	D
004398	02004398	65,035.84	B, D
004560	02004560	143,925.00	D
004813	02004813	197,678.37	D
010345	02900296	125,936.55	A
011451	02900971	98,893.07	A
010776	02900570	86,467.55	A
011798	02901217	80,557.89	D
011036	02900751	75,532.46	A
011538	02901040	72,226.99	D
010052	02900099	62,291.44	B
010579	02900466	53,793.27	A
053140	02006494	56,086.20	D
054419	02008323	99,462.24	D
054424	02008328	172,500.00	D
000413	02000413	294,818.00	F
000000	2005978	55,278.00	E
012072	02201799	400,000.00	A, F
003412	02080819	303,672.09	F
055044	02008081	278,359.51	A, F
055052	02008082	133,932.09	A, F
003467	02080845	126,868.92	E, F
054972	02006363	82,652.69	A, F
005202	02250442	68,300.00	A, F

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

PURCHASES, PAYABLES AND PAYMENTS

Finding Number 02-08: Inadequate Controls over Vouchers for Payment and Related Documents ...(Concluded):

- A – Disbursement vouchers, purchase orders, invoice cancelled paid, supporting documents and quotations or bids were not observed.
- B – Invoice was not cancelled paid.
- C – Deed of purchase was not observed.
- D – Quotations or bids not observed.
- E – Unable to trace to books.
- F – Cancelled checks not observed.

In addition, we found a payment to a supplier in which the withholding of 10% was made twice:

Name of Supplier	Check Date	Check Number	Voucher Number	Amount of Voucher	Description
Professional Contractor Team	4/12/2002	56646	2007242	\$ 326,520	Cert. #25 and #27 Betterments to Mayor Cantera

Criteria:

Chapter IV, Section 12 and 13 of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico, as amended, requires that the Finance Director to keep and safeguard the vouchers, cancelled checks and any other document that justify a payment.

Cause:

The Municipality has inadequate internal controls over retention and the filing of documents due to the lack of an overall control system that provides guidance to the different offices and divisions on the filing and retention requirements of documents.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

PURCHASES, PAYABLES AND PAYMENTS

Finding Number 02-08: Inadequate Controls over Vouchers for Payment and Related Documents ...(Concluded):

Effect:

The Municipality cannot support many of the disbursements made and, therefore, is unable to prove compliance with applicable laws and regulations. In the case of federal funds, the continued occurrence of this situation could result in disallowed cost by the federal awarding agencies and the reduction or elimination of grant awards.

Recommendation:

The Municipality's management should ascertain that adequate source documentation exists to support amounts and items reported as expenditures. The Municipality should also establish a record keeping system to ensure that accounting records and documentation are retained for the time period required by applicable requirements and the provisions of laws, regulations, contracts or grant agreements applicable to the program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

PURCHASES, PAYABLES AND PAYMENTS

FINDINGS NOT REPEATED FROM PRIOR AUDIT

- Finding Number 01-11: Purchase Order prepared after service was received – Our audit procedures did not disclose that purchase orders were prepared after service was received.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

MUNICIPAL LICENSE TAX – REVENUE AND DEFERRED REVENUE

Finding Number 02-09: Lack of Supporting Documentation for Municipal License Taxes Files:

Condition:

During our audit we select a sample of 38 files to examined Volume of Business Declaration – current fiscal year, and a sample of 65 files to examined Volume of Business Declaration – for next fiscal year. In our examination we noted the following situations:

1. Exclusions in the Volume of Business Declaration of taxable income (other income, interests income, subcontracts, etc.), included in the audited financial statements of the taxpayers.
2. Taxpayers that filed extensions for the last year and did not file a final Volume of Business Declaration nor the audited financial statements.
3. Copy of the decree of exemptions is not filed to the corresponding taxpayers.

Criteria:

Chapter IX of the Basic standards establishes the procedures to be followed for filing and collection the municipal license taxes.

Cause:

The Municipality is not properly reviewing the municipal license tax returns when received. In addition, they do not follow up those cases when the taxpayer filed an extension.

Effect:

The continued failure to verify the correctness of the Volume of Business Declarations filed by the taxpayers prevents the Municipality from collecting the correct amount of taxes.

Recommendation:

The Municipality should trained and assign a person to the Municipal License Tax Department that could perform the required procedures and give follow up to taxpayers that did not comply with the law.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING YEAR ENDED JUNE 30, 2002

PAYROLL AND PERSONNEL

Finding Number 02-10: Incomplete Documentation in Employee Files:

Condition:

The Municipality's system of internal control over payroll and personnel is not effectively ensuring the completeness of the employees files. We performed a payroll test where we selected 60 files to be examined. The findings of this test were the followings:

- In a total of 19 files, which represents a 32%, we did not observed the copy of employees' social security card.
- In 24 files of employees, which represents a 40%, the health certificate was not observed.
- In 7 files of employees which represents a 12%, the certificate of good behavior was not observed.
- In 10 files of employees, which represents a 17%, the federal form I-9 was not observed.
- In an employee file, which represents a 2%, the federal form I-9 is not completed in its totality and it is not signed by the employee.
- In 4 files of employees, which represents a 7%, the certificate of birth of the employee was not observed.
- A file of an employee became lost and to the present the new file does not have most of required documents.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

PAYROLL AND PERSONNEL

Finding Number 02-10: Incomplete Documentation in Employee Files ... (Concluded):

Criteria:

The Article 11.023 of the Autonomous Municipalities Law of the Commonwealth of Puerto Rico establishes that the Municipality should maintain a file of its employees that reflects the complete employment record since the initial date on the public service through the date of definitive separation from the service.

Cause:

The Personnel Department failed to obtain the employee documentation required by the Municipality's Regulation.

Effect:

The continued failure to maintain adequate documentation prevent the Municipality from having accurate and complete employee records.

Recommendation:

The Municipality should revise the employee files and require to the employees the information necessary to complete the records.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING
YEAR ENDED JUNE 30, 2002**

PROPERTY MANAGEMENT

FINDINGS NOT REPEATED FROM PRIOR AUDIT

- Finding Number 01-12: Inadequate Controls and Accounting Practices Over the Fixed Assets Subsidiary Ledger - Our audit procedures did not disclose this situation.
- Finding Number 01-13: Lack of Property Physical Inventory – During the fiscal year 2001-02 the Municipality performed a physical inventory of property and equipment for all Municipal departments.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PART IV

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL
OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO FEDERAL PROGRAMS**

- 40 -

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MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

FINDING RELATED TO FEDERAL PROGRAMS THAT HAVE A SEPARATE ACCOUNTING DEPARTMENT AND ADMINISTRATIVE UNIT

Finding Number SA-02-01: Lack of Reconciliation Procedures (Prior Report Finding Number SA-01-01) (First Reported 1988):

Condition:

The Municipality has not established the appropriate system of internal control to ensure the timely and accurate reconciliation of the accounting records maintained by program accountants with those maintained at the Municipality. Funds received from the U.S. Department of Housing and Urban Development for the Community Development Block Grant and Section 8 Clusters; from the U.S. Department of Health and Human Services for the Head Start; and from the U.S. Department of Labor for the Workforce Investment Act and Welfare-to-Work Programs, are managed by their own administrative personnel including their own accounting departments. Each maintains a separate set of accounting records kept on a double entry system. However, the Municipality's central accounting department, has not established the necessary policies and procedures for the reconciliation of the transactions recorded in the Program's accounting records with those recorded in the Municipality's central accounting department.

Criteria:

The Municipality should be aware of its responsibility for administering the grants even though a separate fiscal unit or department is assigned the responsibility of administering the funds.

Cause:

The Finance Director is currently placing reliance upon the accounting records maintained by each of the Programs without having any control procedure to detect inconsistent accounting treatments.

Effect:

This condition results in the possibility of not detecting or preventing errors or irregularities on a timely basis because there is no central oversight of all of the Municipality's financial operations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

**FINDING RELATED TO FEDERAL PROGRAMS THAT HAVE A SEPARATE
ACCOUNTING DEPARTMENT AND ADMINISTRATIVE UNIT**

**Finding Number SA-02-01: Lack of Reconciliation Procedures (Prior Report Finding
Number SA-01-01) (First Reported 1988)...(Concluded):**

Questioned Costs:

None.

Recommendation:

The Municipality should implement monthly reconciliations of the transactions recorded in each of the programs with the transactions processed and recorded in the central accounting department. In addition, it should ensure that all federal financial reports are prepared based on the financial information once reconciled.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG) (CFDA #14.218)

PROGRAM DESCRIPTION

The primary objective of the CDBG Program is the development of viable urban communities, decent housing, suitable living environment, and expanded economic opportunities, principally for persons of low and moderate income. This is to be achieved in two ways. First, funds can only be used to assist eligible activities that fulfill one or more of three national objectives: (1) benefiting low and moderate-income persons; (2) aiding in the prevention or elimination of slums or blight; (3) meeting other community development needs having a particular urgency because existing conditions pose a serious and immediate threat to the health or welfare of the community, and where other financial resources are not available to meet these needs. Secondly, the grantee must spend at least 60% of its funds over a period of up to three years specified by the grantee in its certification for activities that address the national objective of benefiting low- and moderate-income persons.

This Program is conducted by metropolitan cities and urban counties that must submit certain certifications along with a statement as to how they propose using the funds for community development activities. The grant amount is based on a formula that considers the community's population, poverty, extent of overcrowded housing, age of housing, and growth lag.

The CDBG Program also provides for the granting of loan guarantees under HUD Section 108, Loan Guarantee Assistance (LGA). Accordingly, these activities are included as part of the CDBG audit. Findings related to the LGA Section 108 program, if any, will be identified as such.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the CDBG federal financial assistance program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

**Finding Number SA-02-02: Amounts Due from General Fund (Prior Report Finding
Number SA-01-02) (First Reported 1988):**

Condition:

The Municipality has not reimbursed the federal programs for amounts advanced in previous years to the general fund nor is it able to determine the nature and propriety of the differences discussed below. As of June 30, 2002, the Municipality's general fund owed the CDBG program \$392,113. For the fiscal year ended June 30, 2001 the balance was \$1,116,301 of which \$724,188 that was considered as an irreconcilable difference was adjusted.

Criteria:

The Municipality is not in compliance with 24 CFR Section 570.200. The 24 CFR Section 570.200 establishes the eligible activities to be financed with these funds. However, none of the sections under this Title allow the transfer of federal funds to finance the activities of the general fund.

Cause:

The following action caused the above item to occur:

- a) The transfer of federal funds of \$392,113 was due to the failure to prevent the use of federal funds to finance non-federal activities by program and municipal management.

Effect:

This condition permits the financing of the general fund activities with federal funds and places additional financial limitations on the performance of the activities approved under the federal grant. Therefore, this exposes the Municipality to cost disallowance for the amounts owed and may also result in the assessment of penalties and interest costs on amounts owed to the federal programs.

Questioned Costs:

None since this amount has been included as a questioned cost in previous years Single Audit reports.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

**Finding Number SA-02-02: Amounts Due from General Fund (Prior Report Finding
Number SA-01-02) (First Reported 1988) ...(Concluded):**

Recommendation:

The Municipality should seek resolution of this amount with the federal agency. In addition, the Municipality should not permit transfers of federal funds to finance activities not approved by the federal grantor and that are not in accordance with the grant agreements.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-03: Financial Summary Report is Inaccurate (Prior Report Finding Number SA-01-04) (First Reported 1992):

Condition:

The Municipality's system of internal control relating to the preparation of federal financial reports is not effective. The Municipality is not ensuring that the Financial Summary Report ("FSR") submitted to the federal grantor contains accurate financial information. The FSR included within the Consolidated Annual Performance Evaluation Report ("CAPER") for the fiscal year ended June 30, 2002 showed the following errors:

Line on Report	Amount per Report	Amount per Books	Difference
Part II, Line 12 - Disbursed for planning and administration	<u>\$ 1,500,618</u>	<u>\$ 1,338,254</u>	<u>\$ 162,364</u>
Public Services	<u>\$ 768,626</u>	<u>\$ 763,290</u>	<u>\$ 5,336</u>
Total Disbursements	<u>\$ 6,998,431</u>	<u>\$ 6,870,459</u>	<u>\$ 127,972</u>

In addition, the Municipality is not ensuring that the SF-272 Federal Cash Transaction Report submitted to the federal grantor contains accurate financial information. The report as of June 30, 2002 showed the following errors:

Line on Report	Amount per Report	Amount per Books	Difference
Line 11J-Cash on hand end of period	\$ 94,257	\$ 175,659	\$ (81,402)

Criteria:

The 24 CFR Section 85.20 (b)(1) establishes that federal funds recipients shall have a financial management system that will provide for the accurate, current and complete disclosure of the financial results of financially assisted activities.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-03: Financial Summary Report is Inaccurate (Prior Report Finding Number SA-01-04) (First Reported 1992) ...(Concluded):

Cause:

The above differences result from prior year adjustments not being recorded on a timely basis in the accounting books of the Program and/or are due to the lack of reconciliation procedures between the books and financial reports submitted to the federal grantor.

Effect:

The continued occurrence of this situation may result in sanctions by the federal grantor because the information provided in the FSR does not allow them to adequately monitor and evaluate the Program's financial performance.

Questioned Costs:

None.

Recommendation:

Program management should review and corroborate the information included in the FSR before submission to the federal grantor to ensure that all information is accurately presented. In addition, whenever significant adjustments or modifications are deemed necessary, the Municipality should amend submitted reports and include the appropriate supporting explanations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-04: Inadequate Cash Management Procedures (Prior Report Finding Number SA-01-05) (First Reported 1994):

Condition:

The Municipality's internal control over compliance with the cash management requirements of the federal program is not effective since it is not minimizing the time elapsed between the receipt and final disbursement of funds. We selected 30 cash requisitions, and within these requisitions we selected 316 expenditures paid and noted that for 6 of them (2%) the payment was made as follows:

REQUEST VOUCHER NUMBER	DATE OF RECEIPT OF FUNDS	AMOUNT OF FUNDS	CHECK DATE	PASSED WORKABLE DAYS	BENEFICIARY	CHECK NUMBER	AMOUNT
679857	10/3/2001	\$ 754.00	10/25/2001	15	XEROX CORP.	4496	\$ 754.00
679857	10/3/2001	20.66	10/25/2001	15	XEROX CORP.	4489	20.66
679857	10/3/2001	149.00	10/25/2001	15	COMPUTERMASTER	4487	149.00
679857	10/3/2001	1,778.40	10/25/2001	15	THE NEW DAY	4488	1,778.40
683033	10/15/2001	33,999.68	10/19/2001	4	TREASURER M. (IT NAME)	4474-4478	938.05
687143	10/24/2001	5,625.00	1/17/2002	54	CASA PAOLI	5047	3,125.00

Criteria:

The 24 CFR Section 85.20(b)(7) establishes that the federal funds recipient shall adopt the necessary policies and procedures to minimize the time between the receipt of funds and the disbursements for expenditures.

Cause:

The above delays are the result of inadequate cash forecasting procedures because the Municipality has requested and received federal funds in excess of its immediate needs.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

**Finding Number SA-02-04: Inadequate Cash Management Procedures (Prior Report
Finding Number SA-01-05) (First Reported 1994) ...(Concluded):**

Effect:

The continued occurrence of this condition may expose the Municipality to the assessment of interest costs relating to the excess cash on hand which would be paid from local funds.

Questioned Costs:

None.

Recommendation:

The Municipality should modify the cash forecasting process by establishing a system to forecast the cash needs for the next five days, as established by CDBG regulations. Federal funds should only be requested when they are going to be disbursed immediately after receipt, or within three (3) business days.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-05: Unliquidated Obligations of Closed Program Years not Credited to Federal Program (Prior Report Finding Number SA-01-06) (First Reported 1997):

Condition:

The Municipality does not have effective internal controls over compliance with the requirements relating to unliquidated obligations. We noted that as of June 30, 2002, the Municipality has not liquidated its "accounts payable" for the following program years:

<u>Grant Year</u>	<u>Balance</u>
1991	<u>\$23,481</u>

Criteria:

24 CFR Section 85.22(b) establishes that the Municipality should comply with the cost principles included in OMB Circular A-87, paragraph C.4. The Circular establishes that applicable credits refer to those receipts or reduction of expenditure-type transactions that offset or reduce expense items allocable to Federal awards as direct or indirect costs. Examples of such transactions are: purchase discounts, rebates or allowances, recoveries or indemnities on losses, insurance refunds or rebates, and adjustments of overpayments or erroneous charges. To the extent that such credits accruing to or received by the governmental unit relate to allowable costs, they shall be credited to the Federal award either as a cost reduction or cash refund, as appropriate. Since the program years to which these payments are related were already closed, and since these accounts have not changed for several years, the payments should either be made to the corresponding suppliers or credited to the federal grantor for amounts not claimed by suppliers. Therefore, these amounts are considered to be applicable credits to the federal program.

Cause:

The Municipality has not investigated the reasons why the invoices have not been received for the payables encumbered in order to determine whether to issue the corresponding payment or to credit the federal program for amounts that will not be paid.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-05: Unliquidated Obligations of Closed Program Years not Credited to Federal Program (Prior Report Finding Number SA-01-06) (First Reported 1997)...(Concluded):

Effect:

The failure to credit the federal programs with applicable credits may result in cost disallowances since the program was charged for expenditures that will not be paid.

Questioned Costs:

None since this amount has been included as a questioned cost in previous years Single Audit reports.

Recommendation:

The Municipality should reimburse the federal grantor for the above amounts as soon as possible, and adjust its accounting records to eliminate the accounts payable. Furthermore, grant closeout procedures should include the investigation and payment of all grant liabilities or the return of such funds to the federal grantor.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-06: Failure to Monitor Program-Income Producing Activities (Prior Report Finding Number SA-01-07) (First Reported 1997):

Condition:

The Municipality does not have internal controls in place relating to compliance with the requirement to monitor the activities of income producing activities that are funded with Program grants. During our audit over the funds granted for the operations or to other entities, we noted that the Municipality has not established controls to ensure that such funds are being used, together with the corresponding program income that arises from the operation of such entities/facilities, in accordance with program rules and regulations. During the year ended June 30, 2002, the Municipality provided funds to the following entities, which also generated program income from their activities:

Serrallés Castle

Tibes Indian Ceremonial Center

La Perla Theatre

Art and Culture Plaza (Historic Museum)

Cruceta del Vigía

Caribbean Artisan Plaza

Salvador Dijols Basketball Court

Secretariat of Sports and Recreation

Criteria:

The 24 CFR, Part 570.504 and 24 CFR Part 85, Sections 85.20 (b)(1)(2) and 85.21 (f) establish that the grantee must implement the necessary controls for identifying income producing activities, recording and using program income in accordance with applicable grant agreements and regulations.

Cause:

This situation has occurred because the Municipality has not established internal controls to monitor the compliance of these entities/facilities. Also, the Municipality has failed to establish internal controls over financial reporting to ensure that these activities are properly accounted for and recorded in the Municipality's accounting records, as required by federal regulation.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-06: Failure to Monitor Program-Income Producing Activities (Prior Report Finding Number SA-01-07) (First Reported 1997) ...(Concluded):

Effect:

The continued failure to monitor income producing activities may allow funds to be used for ineligible activities exposing the Municipality to cost disallowances for the amounts transferred as well as for program income collected and not used in eligible activities.

Questioned Costs:

Unable to determine since the Municipality does not have separate records to account for these revenues, but it is estimated to exceed \$10,000.

Recommendation:

The Municipality's internal auditor should include monitoring the activities of the aforementioned program-income producing activities within the annual work plan. This should be performed immediately for all years for which funding has been provided to finance these activities. The internal auditor should conclude as to whether the funds were used in accordance with applicable grant provisions and regulations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

Finding Number SA-02-07: Interest Earned Not Remitted to Federal Grantor (Prior Report Finding Number SA-01-09) (First Reported 1987):

Condition:

The Municipality's compliance with the administrative requirement to remit interest earned in excess of \$100 per year on federal fund deposit accounts is not effective. During our audit we noted that the program did not remit to the federal grantor the interest income credited to the CDBG Program cash account as required by federal regulations. The CDBG Program cash account earned interest income of \$9,256 for the fiscal year 2001-2002.

Criteria:

The 24 CFR Section 85.21 (i) establishes that grantees and subgrantees shall promptly, but at least quarterly, remit interest earned on advances to the federal agency. The grantee or subgrantee may keep interest amounts up to \$100 per year for administrative expenses.

Cause:

This occurs because the Municipality has not established internal controls over compliance with the requirement to ensure that any interest earned is promptly remitted to the federal grantor. In addition, another cause for the excess interest earned is the ineffective cash management process of the Municipality because cash requests are made in excess of immediate needs and/or payments are not issued within three days after the receipt of federal funds requirement.

Effect:

The continued failure to comply with this requirement may result in the assessment of interests and penalties from the federal grantor on the amounts owed, as well as the determination of additional restrictions on future funding.

Questioned Costs:

\$9,156 of interest income earned during the year.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

**Finding Number SA-02-07: Interest Earned Not Remitted to Federal Grantor (Prior Report
Finding Number SA-01-09) (First Reported 1987)...(Concluded):**

Recommendation:

The Municipality CDBG Program should reimburse the federal grantor this and other amounts owed in previous years as a result of the same instance of noncompliance. In addition, the Municipality should establish and enforce a monitoring procedure within the Program to ensure that interest earned in excess of \$100 is remitted on a quarterly basis.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

COMMUNITY DEVELOPMENT BLOCK GRANT (CDBG)

FINDINGS NOT REPEATED FROM PRIOR AUDIT

- Finding Number SA-01-03: Unsupported Difference in Bank Reconciliation – Our audit procedures did not disclose any unsupported difference in the bank reconciliation.
- Finding Number SA-01-08: Inadequate Property Management Procedures - Our audit procedures did not disclose that were inadequate property management procedures.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

SECTION 8 – HOUSING CHOICE VOUCHER (CFDA # 14.871)

PROGRAM DESCRIPTION

The Section 8 Housing Choice Voucher (HCVP) objectives are to provide rental assistance to help very low-income families afford decent, safe and sanitary rental housing. The subsidy provided by the Program is considered tenant-based subsidy because when an assisted family moves out of a unit leased under the Program, the assistance contract with the owner terminates and the family may move to another unit with continued rental assistance.

Under the Housing Choice Voucher Program, apart from the requirement that the rent must be reasonable in relation to rents charged for comparable units in the private unassisted market, there is no limit on the amount of rent that an owner may charge for a unit. However at initial occupancy of any unit where the gross rent exceeds the payment standard, a family may not pay more than 40 percent of adjusted monthly income toward rent and utilities. Voucher subsidy is set based on the difference between the PHA's applicable payment standard for the family or the gross rent and the total tenant payment (generally 30 percent of the family's monthly-adjusted income). This is the maximum amount of subsidy a family may receive regardless of the rent the owner charges for the unit. The approximate number of participants during the year ended June 30, 2002 for the program was 1,488.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to these federal financial assistance programs.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

SECTION 8 – HOUSING CHOICE VOUCHER

Finding Number SA-02-08: Inadequate Cash Management Procedures (Prior Report Finding Number SA-01-10) (First Reported 1987):

Condition:

The Municipality's internal control over compliance with the cash management requirements of the federal program is not effective since it is holding excessive cash balances in its bank accounts. During our audit of the bank reconciliations of the Program cash accounts, we noted that the average balance on hand significantly exceeded the average cash need of the Program. Following is a list of the average balances of cash on hand for the Program, as well as during the fiscal year:

Month Ended	Deposits	Disbursements	Transfers to Other Programs	Bank Balance
July 31, 2001	\$ 8,916	\$ 427,358	\$ 127,359	\$ 1,045,436
August 31, 2001	1,314,255	549,785	116,241	1,693,665
September 30, 2001	12,260	480,792	94,594	1,130,540
October 31, 2001	636,210	473,137	93,486	1,200,125
November 30, 2001	1,203,854	947,518	99,485	1,356,977
December 31, 2001	430,256	490,829	112,995	1,183,410
January 31, 2002	630,517	541,572	100,099	1,172,255
February 28, 2002	601,306	486,176	110,643	1,176,742
March 31, 2002	1,463,541	504,884	94,095	2,041,305
April 30, 2002	10,229	537,562	97,507	1,416,466
May 31, 2002	1,203,354	573,410	94,972	1,951,437
June 30, 2002	12,571	529,745	86,863	1,347,400
Average balance	<u>\$ 627,273</u>	<u>\$ 545,231</u>	<u>\$ 102,362</u>	<u>\$ 1,392,980</u>

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

SECTION 8 – HOUSING CHOICE VOUCHER

**Finding Number SA-02-08: Inadequate Cash Management Procedures (Prior Report
Finding Number SA-01-10)(First Reported 1987)...(Concluded):**

Criteria:

The 24 CFR Section 85.20(b)(7) establishes that the federal funds recipient shall adopt the necessary policies and procedures to minimize the time elapsing between the receipt of funds and their disbursement for expenditures.

Cause:

The above conditions are the result of inadequate cash forecasting procedures since the Municipality has requested and received federal funds in excess of its immediate needs since there is cash on hand to cover future needs.

Effect:

The continued occurrence of this condition may expose the Municipality to the assessment of interest costs on the excess cash on hand, which would be paid from local funds.

Questioned Costs:

None.

Recommendation:

The Municipality should use cash on hand before requesting additional funds.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

SECTION 8 – HOUSING CHOICE VOUCHER

Finding Number SA-02-9: Amounts Due from General Fund (Prior Report Finding Number SA-01-11) (First Reported 1992):

Condition:

The Municipality has not reimbursed the federal program for the federal funds used to finance the general fund's activities. As of June 30, 2002, a balance of \$1,268,349 remained outstanding for funds that were transferred to the Municipality's general fund in prior years. The transfer represents an instance of noncompliance with an executive order issued by the Mayor in August 1992.

Criteria:

The 24 CFR Section 570.200 establishes the various allowable activities to be financed with federal funds. However, none of the sections under this Title allows the transfer of federal funds to finance the activities of the general fund.

Cause:

The Department of Finance failed to monitor and control transfers of federal funds to general fund, which were realized without the proper authorization from the federal grantor.

Effect:

This condition permits the financing of the general fund activities with federal funds and places additional financial limitation on the performance of the activities approved under the federal grant. Accordingly, the continued failure to reimburse the federal program may expose the Municipality to the assessment of interest costs and penalties in relation to the use of these funds.

Questioned Costs:

None since this amount has been included as a questioned cost in previous years Single Audit reports.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

SECTION 8 – HOUSING CHOICE VOUCHER

Finding Number SA-02-9: Amounts Due from General Fund (Prior Report Finding Number SA-01-11) (First Reported 1992)...(Concluded):

Recommendation:

The general fund must reimburse the federal program the amount owed as soon as possible. In addition, the Municipality should not permit transfers of federal funds to finance activities not approved by the Federal grantor and that are not in accordance with the grant agreements.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

SECTION 8 – HOUSING CHOICE VOUCHER

Finding Number SA-02-10: Inadequate Documentation of Participant Files Procedures (Prior Report Finding Number SA-01-13) (First Reported 1986):

Condition:

The Municipality's system of internal control over compliance with the documentation of participant files is not working effectively. During our audit of the participant files in the Section 8 program, we noted that the Municipality was not maintaining the required documents and information in each file to support participant's eligibility as required by Section 8 Program regulations. During our tests of eligibility requirements, we tested twenty-five (25) participant files and noted the following exceptions:

Contract #	Monthly Amount	1	2
Vouchers 00-653-2V	\$ 425.00	X	
Vouchers 99-294-2V	503.00		X
Vouchers 02-390-V	350.00		X
Vouchers 99-295-2V	300.00		X
Total instances of noncompliance		1	3
Sample size		25	25
Percentage of noncompliance		4%	12%
Questioned Costs		None	None

1. The inspector made findings that had to be corrected and in the report of quality standards it is not possible to be determined if they were corrected, even though was specified in the report that had passed inspection.
2. There was one comparable for each house, instead of the three comparables required.

Criteria:

24 CFR Sections 882-113, 882-209, 882-214, 882-412, 882-514, 882-515, 882-518, 883-711, 883-704, and 889-103 establish that the PHA is required to accept applications for admission to the projects, determine whether the applicants are initially eligible, and on a yearly basis, reexamine family income, composition, and contribution to rent and utilities. In addition, the Municipality should verify that the information submitted by participants is reliable.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

SECTION 8 – HOUSING CHOICE VOUCHER

Finding Number SA-02-10: Inadequate Documentation of Participant Files ...(Concluded):

Cause:

All of the above matters occur because the Municipality's system of internal control relating to the compliance requirements is not effectively identifying and correcting these matters through the proper review of participant files for completeness of documents, signatures and information, as well as for their accuracy. The current procedures do not effectively reduce the risk of ineligible participants receiving program benefits.

Effect:

The continued failure to establish internal control over compliance with the above requirements exposes the Municipality to unauthorized user or disposition of the program's resources.

Questioned Costs:

None.

Recommendation:

The Municipality should design and adopt a checklist that includes all the related documents that must be completed for each participant file. The checklist should be completed during the initial processing and revised for changes during the annual review. Once completed, the participant files should then be reviewed for completeness by another official or supervisor prior to the final approval. These procedures will help to improve controls and documentation concerning the eligibility of participants and will reduce the possibility of cost disallowances.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

SECTION 8 – HOUSING CHOICE VOUCHER

FINDING NOT REPEATED FROM PRIOR AUDIT

- Finding Number SA-01-12: Ineffective Property Management Controls – Our procedures for the current year did not indicate a lack of compliance.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

SECTION 8 - PROJECT BASED CLUSTER LOWER INCOME HOUSING ASSISTANCE PROGRAM – SECTION 8 MODERATE REHABILITATION I & II (CFDA # 14.856)

PROGRAM DESCRIPTION

The Moderate Rehabilitation Program assists low income families in affording decent, safe and sanitary housing by encouraging property owners to rehabilitate substandard housing and lease the units with rental subsidies to low income families. The Public Housing Authority (PHA) and the owner execute an Agreement to Enter into Housing Assistance Payments Contract under which the owner agrees to rehabilitate the unit to be subsidized and the PHA agrees to subsidize the units upon satisfactory completion of rehabilitation. Upon completion of the rehabilitation, the PHA and the owner execute a HAP contract. The PHA refers interested eligible families on its Section 8 waiting list to the owner to fill vacancies in moderate rehabilitation units.

The Moderate Rehabilitation Program assistance is considered a project-based subsidy because the assistance is tied to specific units under an assistance contract with the owner for a specified term. A family that moves from a unit with project-based assistance does not have any right to continued assistance.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to these federal financial assistance programs.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

**SECTION 8 – PROJECT BASED CLUSTER
LOWER INCOME HOUSING ASSISTANCE PROGRAM –
SECTION 8 MODERATE REHABILITATION I & II**

FINDING NOT REPEATED FROM PRIOR AUDIT

- Finding Number SA-01-14: Inadequate Cash Management Procedures - Our audit procedures for the current year did not indicate a lack of compliance.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HUD DISASTER RECOVERY INITIATIVE (GRANT NO. B-98MU-72-0003)

PROGRAM DESCRIPTION

HUD's Disaster Recovery Initiative helps communities impacted by disasters receiving Presidential declarations. HUD Disaster Recovery funds are intended to support the activities of other Federal agencies and cannot be used for activities reimbursable or for which funds are made available by the Federal Emergency Management Agency (FEMA), the Small Business Administration (SBA), or the U.S. Army Corps of Engineers (USACE).

An objective of the program is the redevelopment of viable urban communities, by providing decent housing and a suitable living environment and expanding economic opportunities, especially for persons of low and moderate income.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the Public Assistance federal financial assistance program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HUD DISASTER RECOVERY INITIATIVE

Finding Number SA-02-11: Inadequate Cash Management Procedures (Prior Report Finding Number SA-01-16) (First Reported 2001):

Condition:

The Municipality's internal controls relating to compliance with the cash management requirements of the federal program are not effective since they are not minimizing the time elapsed between the receipt and final disbursement of funds. We selected our sample from the months of July 2001, and October 2001, and found that the Municipality did not disburse the funds within the period of three (3) days workable after the Municipality received the funds. We observed this situation in the following cases:

<u>VOUCHER NUMBER</u>	<u>DATE OF RECEIPT OF FUNDS</u>	<u>AMOUNT OF FUNDS</u>	<u>CHECK DATE</u>	<u>PASSED WORKABLE DAYS</u>	<u>BENEFICIARY</u>	<u>CHECK NUMBER</u>	<u>AMOUNT</u>
002-162330	10/25/02	\$ 1,239.25	11/01/01	5	Commercial San Jose	254	\$ 1,239.25
002-162330	10/25/02	19,132.50	11/05/01	7	Caguas Lumber Yard	257	19,132.50
		<u>\$ 20,371.75</u>					<u>\$ 20,371.75</u>

Criteria:

24 CFR Section 85.20(b)(7) establishes that the federal funds recipient shall adopt the necessary policies and procedures to minimize the time elapsing between the receipt of funds and the disbursements for expenditures.

Cause:

The above exceptions are the result of inadequate cash forecasting procedures since the Municipality has requested and received federal funds in excess of its immediate needs.

Effect:

The continued occurrence of this condition may expose the Municipality to the assessment of interest costs over the excess cash on hand, which would be paid from local funds.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HUD DISASTER RECOVERY INITIATIVE

**Finding Number SA-02-11: Inadequate Cash Management Procedures (Prior Report
Finding Number SA-01-16) (First Reported 2001)...(Concluded):**

Questioned Costs:

None.

Recommendation:

The Municipality should modify the cash forecasting process of the program by establishing a system to forecast the cash needs for its immediate needs, as established by federal regulations. Federal funds should only be requested when they are going to be disbursed immediately after receipt.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HUD DISASTER RECOVERY INITIATIVE

Finding Number SA-02-12: Noncompliance with the Period of Availability of Federal Funds (Prior Report Finding Number SA-01-17) (First Reported 2001):

Condition:

The Municipality is not obligating federal funds within the required obligation period established by federal regulations. Our test of expenditures revealed that several transactions were made after the required obligation period as follows:

Voucher Number	Voucher Date	Expenditure Amount	Description	Obligation Date	Obligation Due Date
02-38-017	8/16/2001	\$ 11,797.76	Construction materials	August 18, 2001	December 1, 2000
02-38-018	8/22/2001	124.70	Construction materials	August 19, 2001	December 1, 2000
02-38-019	8/22/2001	19,840.70	Construction materials	August 19, 2001	December 1, 2000
		31,763.16			
02-38-029	7/17/2001	1,695.00	Construction materials	October 23, 2001	December 1, 2000
02-38-030	7/17/2001	635.47	Construction materials	October 23, 2001	December 1, 2000
		2,330.47			
02-38-035	10/9/2001	1,239.25	Construction materials	October 23, 2001	December 1, 2000
02-38-035	10/9/2001	1,239.25	Construction materials	October 29, 2001	December 1, 2000
02-38-036	10/17/2001	19,132.50	Construction materials	October 23, 2001	December 1, 2000
02-38-041	10/23/2001	601.75	Construction materials	November 15, 2001	December 1, 2000
02-38-037	10/17/2001	2,003.00	Construction materials	November 16, 2001	December 1, 2000
02-38-040	10/23/2001	179.53	Construction materials	November 16, 2001	December 1, 2000
02-38-042	10/23/2001	12,281.00	Construction materials	November 16, 2001	December 1, 2000
02-38-043	10/23/2001	239.00	Construction materials	November 16, 2001	December 1, 2000
02-38-048	10/30/2001	2,982.05	Construction materials	November 16, 2001	December 1, 2000
02-38-049	10/30/2001	4,323.20	Construction materials	November 16, 2001	December 1, 2000
		44,220.53			
Total		<u>\$ 78,314.16</u>			

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HUD DISASTER RECOVERY INITIATIVE

Finding Number SA-02-12: Noncompliance with the Period of Availability of Federal Funds (Prior Report Finding Number SA-01-17) (First Reported 2001) ...(Concluded):

Criteria:

The Special Contract Conditions Applicable to the Use of HUD Disaster Recovery Initiative Funds establish that all Disaster Recovery Initiative Funds must be obligated within twenty-four (24) months of the effective date of the grant agreement.

Cause:

The above condition occurred because the Municipality has not taken the appropriate steps to ensure federal fund disbursements are made within the period of availability.

Effect:

The failure to obligate such funds within the allowed time period may result in cost disallowed by the federal grantor.

Questioned Cost:

None.

Recommendation:

The Municipality should improve its internal control procedures to ensure federal funds are obligated within the required time period.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HUD DISASTER RECOVERY INITIATIVE

Finding Number SA-02-13: Ineffective Controls Over Preparation and Submission of Federal Financial Reports (Prior Report Finding Number SA-01-18) (First Reported 2001):

Condition:

The Municipality does not have effective internal controls to ensure the accurate preparation and timely submission of federal financial reports of the Program. We noted the following differences:

	<u>Line</u>	<u>Amount per Books</u>	<u>Amount per Report</u>	<u>Difference</u>
<u>Performance Reports:</u>				
<u>Quarter Ended</u> September 30, 2001	Total cumulative expenditures	\$ 3,122,074	\$ 4,033,289	\$ (911,215)
<u>Quarter Ended</u> December 31, 2001	Total cumulative expenditures	4,547,377	4,565,604	(18,227)
<u>Quarter Ended</u> March 31, 2002	Total cumulative expenditures	4,555,511	4,571,672	(16,161)
<u>Quarter Ended</u> June 30, 2002	Total cumulative expenditures	4,550,561	4,580,972	(30,411)

Criteria:

The 24 CFR Section 85.20 (b)(1) establishes that federal funds recipients shall have a financial management system that will provide for the accurate, current and complete disclosure of the financial results of federally assisted activities.

Cause:

The exceptions described above result from the preparation of federal financial reports without ensuring that the amounts reported agree with the underlying accounting records, and the failure of management to detect these differences during their review and approval of the federal financial reports. The continued failure to file accurate financial reports may result in actions by the federal grantor against the Municipality, such as grant payment withholdings resulting from the misstatement of the financial performance of the program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HUD DISASTER RECOVERY INITIATIVE

**Finding Number SA-02-13: Ineffective Controls Over Preparation and Submission of
Federal Financial Reports (Prior Report Finding Number SA-01-18) (First Reported 2001)
...Concluded):**

Effect:

The continued occurrence of this situation may result in sanctions by the federal grantor because the information provided in the performance reports does not allow them to adequately monitor and evaluate the Program's financial performance.

Questioned Costs:

None.

Recommendation:

The reviewer of these reports should ensure that amounts reported agree with the underlying accounting records before submission to the federal grantor. In addition, whenever significant adjustments or modifications are deemed necessary, the Municipality should amend submitted reports and include the appropriate supporting explanations.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HUD DISASTER RECOVERY INITIATIVE

Finding Number SA-02-14: Noncompliance with Earmarking Requirements:

Condition:

The Municipality does not have effective internal control system over compliance with earmarking requirement established by federal grantor. The Municipality should expend the total grant amount in thirty-six months.

Grant Year	Total Grant	Total Funds Expended in 36 Months
GRANT NO.: B- 98-MU-72-0003	\$ 4,590,285.00	
1998-99		\$ 98,455.34
1999-00		630,352.63
2000-01		<u>1,329,562.17</u>
		<u>\$2,058,370.14</u> 45%

Criteria:

Of the HUD Disaster Recovery Initiative funds made available under this Grant Agreement, all amounts, except those amounts budgeted for planning and administrative cost activities or those amounts being carried out under force account, shall be obligated (under contractual obligations) within twenty-four (24) months of the effective date of this Grant Agreement. All amounts under this Grant Agreement must be expended with thirty-six (36) months of the effective date of this Grant Agreement.

Cause:

This situation is cause due to the failure to obligate and expend the federal funds as per required by the Grant Agreement.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HUD DISASTER RECOVERY INITIATIVE

**Finding Number SA-02-14: Noncompliance with Earmarking Requirements
...(Concluded):**

Effect:

The Department of Housing and Urban Development may reduce the grantee's line of credit by any amount not meeting these conditions and reallocate such amounts to other grantees for disaster recovery activities.

Questioned Costs:

None.

Recommendation:

Program management should obligate and expend funds as established in the Grant Agreements.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

WORKFORCE INVESTMENT ACT CLUSTER ("WIA") WORKFORCE INVESTMENT ACT – ADULT PROGRAM (CFDA # 17.258) WORKFORCE INVESTMENT ACT – YOUTH ACTIVITIES (CFDA # 17.259) WORKFORCE INVESTMENT ACT – DISLOCATED WORKERS (CFDA # 17.260)

PROGRAM DESCRIPTION

The Workforce Investment Act of 1998 (WIA) reforms Federal job training programs and creates a new, comprehensive workforce investment system. The reformed system is intended to be customer-focused, to help Americans access the tools they need to manage their careers through information and high quality services, and to help U.S. companies find skilled workers. The cornerstone of the new workforce investment system is One-Stop service delivery, which unifies numerous training, education and employment programs into a single, customer-friendly system in each community so that the customer has access to a seamless system of workforce investment services.

There are three program categories under Subtitle B of Title I: Adult; Dislocated Worker; and Youth Activities. Programs for adults and dislocated workers seek to improve employment, retention, and earnings of WIA participants and increase their educational and occupational skill attainment, thereby improving the quality of the workforce, reducing welfare dependency, and enhancing national productivity and competitiveness. Subtitle B Youth activities seek to increase the attainment of basic skills, work readiness or occupational skills, and secondary diplomas or other credentials.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the Workforce Investment Act financial assistance program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

WORKFORCE INVESTMENT ACT CLUSTER ("WIA")

Finding Number SA-02-15: Inadequate Cash Management Procedures (Prior Report Finding Number SA-01-20) (First Reported 2001):

Condition:

The Municipality's internal controls relating to compliance with the cash management requirements of the federal program are not effective since they are not minimizing the time elapsed between the receipt of funds and final disbursement for payment.

07/31/01	\$ 1,904,779.78	\$ 1,049,893.19	\$ 682,125.28
08/31/01	837,013.86	999,589.19	519,549.95
09/30/01	620,602.81	1,256,297.89	(116,145.13)
10/31/01	953,832.88	496,649.37	341,038.38
11/30/01	383,601.09	435,968.36	288,671.11
12/31/01	423,204.40	410,913.25	300,962.26
01/31/02	486,405.32	453,809.24	333,558.34
02/28/02	526,305.28	363,782.19	496,081.43
03/31/02	1,579,128.10	1,704,530.09	370,679.44
04/30/02	506,974.36	503,713.73	373,940.07
05/31/02	614,122.46	690,576.78	297,485.75
06/30/02	1,637,901.13	1,222,693.41	712,693.47
	<u>\$ 10,473,871.47</u>	<u>\$ 9,588,416.69</u>	

Average Monthly Balance

\$ 383,386.70

Criteria:

The WIA Fiscal and Cash Management Guide issued by the Council establishes that the Program's cash on hand balance shall not exceed a 5-day need.

Cause:

The above condition occurred because the Program's cash requisitions are made to cover the total disbursements for the month and not for its immediate needs. The Program has adopted this approach due to the delay of the Technological Occupational Education Council (the "Council") in disbursing the funds requested by the Program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

WORKFORCE INVESTMENT ACT CLUSTER ("WIA")

**Finding Number SA-02-15: Inadequate Cash Management Procedures (Prior Report
Finding Number SA-01-20) (First Reported 2001) ...(Concluded):**

Effect:

The continued occurrence of this condition may expose the Municipality to the assessment of interest costs relating to the excess cash on hand, which could be paid from local funds.

Questioned Costs:

None.

Recommendation:

The Municipality should modify the cash forecasting process by establishing a system to forecast the cash needs for the next five days, as established by the WIA regulations. Federal funds should only be requested when they are going to be disbursed immediately after receipt or within the next five business days.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

**ADMINISTRATION FOR CHILDREN, YOUTH AND FAMILIES
("HEAD START") (CFDA # 93.600)**

PROGRAM DESCRIPTION

The objectives of the Head Start Program are to provide comprehensive health, educational, nutritional, social, and other services to economically disadvantaged pre-school children so that the children will attain overall social competence. Parents also participate in various decision-making processes related to the operation of the program.

Grants are made by the Administration for Children, Youth and Families, ("ACYF"), to community action agencies, limited purpose agencies and units of local government who operate the program or assign the activity to one or more delegate agencies identified in the grant application. Each grantee and delegate agency generally operates the program through several locations.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the Head Start federal financial assistance program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HEAD START PROGRAM

Finding Number SA-02-16: Ineffective Controls Over Preparation and Submission of Federal Financial Reports (Prior Report Finding Number SA-01-21) (First Reported 1986):

Condition:

The Municipality does not have effective system of internal control to ensure the accurate preparation and timely submission of federal financial reports of the Program. We noted the following differences:

<u>Federal Cash Transactions Reports:</u>	<u>Line</u>	<u>Amount per Books</u>	<u>Amount per Report</u>	<u>Difference</u>
<u>Quarter Ended</u>				
September 30, 2001	Cash on hand - beginning of period	\$ 139,199	\$ 158,584	\$ (19,385)
	Total cash available		2,395,664	
	Net disbursements		2,554,248	
	Cash on hand - end of period		(2,823,952)	
		133,526	(269,704)	403,230
<u>Quarter Ended</u>				
December 31, 2001	Cash on hand - beginning of period	133,526	(269,704)	403,230
	Total cash available		2,959,242	
	Net disbursements		2,689,538	
	Cash on hand - end of period		(3,076,499)	
		17,247	(386,961)	404,208
<u>Quarter Ended</u>				
March 31, 2002	Cash on hand - beginning of period	17,247	(386,961)	404,208
	Total cash available		2,807,703	
	Net disbursements		2,420,743	
	Cash on hand - end of period		(2,865,601)	
		(40,344)	(444,858)	404,514
<u>Quarter Ended</u>				
June 30, 2002	Cash on hand - beginning of period	(40,344)	981,410	(1,021,754)
	Total cash available		3,740,635	
	Net disbursements		4,722,045	
	Cash on hand - end of period		(3,803,826)	
		(96,828)	918,219	(1,015,047)

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HEAD START PROGRAM

Finding Number SA-02-16: Ineffective Controls Over Preparation and Submission of Federal Financial Reports (Prior Report Finding Number SA-01-21) (First Reported 1986) ... (Concluded):

Criteria:

45 CFR Section 92.41-(b)(3) requires federal fund recipients to periodically monitor the performance of grant-supported activities to assure that time schedules are being met, projected work units by time periods are being accomplished, and other performance goals are being achieved by the preparation of federal financial reports. To achieve these goals, management shall prepare accurate and timely federal financial reports. In addition, Common Rule, Paragraph 20-(b)(1) establishes that federal fund recipients shall have a financial management system that will provide for the accurate, current and complete disclosure of the financial results of financially assisted activities. The same shall be the underlying record to support the amounts included in the financial reports submitted to federal grantor. Also, 45 CFR Section 74.74 states that the Federal Cash Transaction Report must be submitted no later than 45 working days following the end of each quarter.

Cause:

The conditions described above result from the preparation of federal financial reports without ensuring that the amounts reported agree with the underlying accounting records, and the failure of management to detect these differences during their review and approval of the federal financial reports.

Effect:

The continued failure to file accurate financial reports may result in actions by the federal grantor against the Municipality, such as grant payment withholdings resulting from the misstatement of the financial performance of the program.

Questioned Costs:

None.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HEAD START PROGRAM

Finding Number SA-02-16: Ineffective Controls Over Preparation and Submission of Federal Financial Reports (Prior Report Finding Number SA-01-21) (First Reported 1986) ... (Concluded):

Recommendation:

The reviewer of these reports should ensure that amounts reported agree with the underlying accounting records before submission to the federal grantor. Also, the Municipality should implement a reporting calendar to keep all personnel aware of the reporting deadlines of each federal financial report. This will provide an additional tool to help the Municipality in complying with the required reporting deadlines.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

Finding Number SA-02-17: Failure to Meet Full Enrollment Level (Prior Report Finding Number SA-01-22) (First Reported 1986):

Condition:

The Municipality is not achieving the necessary enrollment levels for the Program. The Program did not maintain a full enrollment for the academic year ended December 31, 2001 as required by the funding agreement with the Federal grantor. The total funded (required) enrollment and actual enrollment were as follows:

	Head Start	Early Head Start
Total funded enrollment for the year (required enrollment)	1,580	72
Total actual enrollment for period ended December 31, 2001	<u>1,524</u>	<u>24</u>
Enrollment not met	<u>56</u>	<u>48</u>

Criteria:

45 CFR Part 1305, establishes that enrollment is an on-going process, and maintenance of a full enrollment level depends upon the success of the recruitment program. The Head Start Program must maintain an enrollment level equal to its funded slots and must try to fill vacancies as soon as they occur in order to maintain full enrollment. All vacancies must be filled within 30 calendar days.

Cause:

This exception results because the Municipality is requesting funding for the enrollment of 1,580 for Head Start participants and 72 for Early Head Start participants, while available facilities can only hold a maximum of 1,524 and 24 participants, respectively. In addition full enrollment is not achieved at all locations.

Effect:

The failure to comply with the required enrollment level may result in cost disallowances by the federal grantor since cost per child served exceeds the budgeted cost per child based on the funded enrollment approved.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HEAD START PROGRAM

**Finding Number SA-02-17: Failure to Meet Full Enrollment Level (Prior Report Finding
Number SA-01-22) (First Reported 1986) ...(Concluded):**

Questioned Costs:

\$322,851 – Calculated as follows:

	Early Head Start
Approved grant for calendar year ended December 31, 2001, net of administrative costs	\$ 658,901
Funded enrollment per proposal	÷ <u>72</u>
Average budgeted direct cost per participant	\$ 9,151
Actual expenditures incurred under the grant-year ended December 31, 2001, net of administrative costs	\$ 542,484
Actual enrollment	÷ <u>24</u>
Actual average direct cost per participant	<u>22,604</u>
Excess direct cost per participant	\$ 13,452
Actual participants	× <u>24</u>
Questioned costs	<u>\$ 322,851</u>

Recommendation:

The Municipality should obtain additional facilities in order to be able to meet the full enrollment level or reduce the funding requirement, when requesting funds. Also, the Municipality should consider evaluating the effectiveness of the enrollment process at those locations where full enrollment is not met, and either close the facilities or change location to an area where full enrollment can be met.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HEAD START PROGRAM

Finding Number SA-02-18: Inadequate Cash Management Procedures (Prior Report Finding Number SA-01-23) (First Reported 1986):

Condition:

The Municipality's internal controls relating to compliance with the cash management requirements of the federal program are not effective since they are not minimizing the time elapsed between the receipt and final disbursement of funds. We selected 21 cash requisitions, totaling \$1,075,689 and noted that the Municipality is holding funds in excess of three-days worth of payments as follows:

<u>Amount Requested</u>	<u>Date Received</u>	<u>Disbursed within 4 - 10 days</u>	<u>Total Noncompliance</u>
\$ 384,981	December 20, 2001	\$ 4,746	\$ 4,746
395,318	March 22, 2002	388,272	388,272
438,739	May 10, 2002	1,135	1,135
<u>438,739</u>	May 10, 2002	<u>4,840</u>	<u>4,840</u>
<u>\$ 1,657,777</u>		<u>\$ 398,994</u>	<u>\$ 398,994</u>

Criteria:

The 45 CFR Section 92.20(b)(7) establishes that the federal funds recipient shall adopt the necessary policies and procedures to minimize the time elapsing between the receipt of funds and the disbursements for expenditures. For this program, the cash on hand should not exceed three-day worth of expenditures.

Cause:

The above conditions are the result of inadequate cash forecasting procedures since the Municipality has requested and received federal funds in excess of its immediate needs. The continued occurrence of this condition may expose the Municipality to the assessment of interest costs on the excess cash on hand, which would be paid from local funds.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

**FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS
YEAR ENDED JUNE 30, 2002**

HEAD START PROGRAM

**Finding Number SA-02-18: Inadequate Cash Management Procedures (Prior Report
Finding Number SA-01-23) (First Reported 1986) ...(Concluded):**

Effect:

The continued occurrence of this condition may expose the Municipality to the assessment of interest costs over the excess cash on hand.

Questioned Costs:

None.

Recommendation:

The Municipality should modify the cash forecasting process of the program by establishing a system to forecast the cash needs for the next three days, as established by federal regulations. Federal funds should only be requested when they are going to be disbursed immediately after receipt.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HEAD START PROGRAM

Finding Number SA-02-19: Failure to Meet the Minimum Required Average Daily Attendance Level (Prior Report Finding Number SA-01-24) (First Reported 1995):

Condition:

The Municipality did not comply with the requirement of the grantor of 85% of attendance rate. We selected 17 out of 77 Head Start Centers and for each center we examined the report summary of assistance for the year. The Municipality did not achieve the required minimum daily attendance rates for 10 out of 17 of the Head Start Centers selected for testing. For 10 of the 17 daily attendance records examined the Municipality did not comply with the requirement of the grantor of 85% of attendance rate.

<u>Center</u>	<u>Date</u>	<u>Days Center Was in Operation</u>	<u>Enrollment</u>	<u>Average Daily Attendance Rate</u>	<u>Required Attendance Rate 85%</u>
Aristides Chavier 1	12/31/2001	173	20	80%	Not Comply
Aristides Chavier 2	12/31/2001	173	22	81%	Not Comply
Aristides Chavier 3	12/31/2001	173	20	78%	Not Comply
Jardines del Caribe 1	12/31/2001	173	21	78%	Not Comply
Jardines del Caribe 2	12/31/2001	173	21	79%	Not Comply
Las Americas 1	12/31/2001	173	20	82%	Not Comply
Las Americas 2	12/31/2001	173	20	82%	Not Comply
Magueyes 1	12/31/2001	173	21	74%	Not Comply
Magueyes 2	12/31/2001	173	20	83%	Not Comply
Ponce Centro 2	12/31/2001	173	22	84%	Not Comply
Villa Paraiso 1	12/31/2001	173	22	76%	Not Comply
Villa Paraiso 2	12/31/2001	173	21	78%	Not Comply
Villa Paraiso 3	12/31/2001	173	21	81%	Not Comply

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

FINDINGS ON COMPLIANCE AND ON INTERNAL CONTROL OVER COMPLIANCE WITH REQUIREMENTS APPLICABLE TO FEDERAL PROGRAMS YEAR ENDED JUNE 30, 2002

HEAD START PROGRAM

Finding Number SA-02-19: Failure to Meet the Minimum Required Average Daily Attendance Level ... (Concluded):

Criteria:

The Head Start Enrollment and Attendance Policies, Federal Register, Vol. 44, No. 214, requires a minimum average daily attendance of 85%. In addition, 45 CFR 92.41-(b)(3) requires federal fund recipients to periodically monitor the performance of grant-supported activities to assure that time schedules are being met, projected work units by time periods are being accomplished, and other performance goals are being achieved.

Cause:

The failure to meet this requirement results from the failure to assess the reasons for participant absenteeism, and for the need to provide additional incentives to increase and maintain the attendance level.

Effect:

The continued failure to meet the required attendance levels may result in cost disallowances or in the reduction of future grant awards because this situation may be an indicator of needed improvements in service delivery and consequently, the overall program objectives may not be consistently met. In addition, federal funds spent per participant may be substantially higher than the proposed cost per participant, thus exposing the Municipality to cost disallowances as a result of excess costs incurred in relation to the participants enrolled.

Questioned Costs:

None determined because we already assessed questioned costs in Finding Number SA-02-17 for not meeting minimum enrollment level.

Recommendation:

The program should analyze the specific causes for absenteeism. Such analysis shall include, but not be limited to, a study of the absence pattern for each child and hold meetings with parents/guardians to provide orientation as to the benefits of daily attendance. In addition, the program should initiate the corresponding action based on the results of the analysis.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PART V

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

- 89 -

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

The following findings and recommendations arise from our follow-up procedures of material instances of noncompliance noted during the Single Audit for the year ended June 30, 2001. These programs were not audited as major programs during our 2002 audit because these did not meet the audit requirements established by OMB Circular A-133.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

PUBLIC ASSISTANCE GRANTS

Finding Number SA-02-20: Lack of Formal Accounting Records to Support Federal Financial Reports:

Condition:

The Municipality does not maintain a self-balancing set of accounts or any type of formal accounting records to account for the transactions and payments of the Program. The Program does not maintain a formal set of books and accounts. Instead, spreadsheet-based records support accounting and reporting. Therefore, the Program does not have current accurate and complete information with regard to the Programs' assets, liabilities, obligations, unobligated balances, nor is there proper accountability and internal control at Program level for the assets owned. In addition, there is no accurate comparison of actual expenditures against budgeted amounts at the account level.

Criteria:

The 45 CFR Section 92.20(b)(2) establishes that grantees and subgrantees must maintain records that 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. Furthermore, Section 20(b)(3) establishes that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Also, Section 20(b)(4) establishes that actual expenditures or outlays must be compared with budgeted amounts for each grant or subgrant.

Cause:

This has occurred because the Municipality has exercised inadequate oversight over the accounting functions of this program by not requiring the establishment of a separate set of books for this program. Instead, the Municipality has permitted the maintenance of informal accounting records, such as spreadsheets, to support the accountability of a major federal program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

PUBLIC ASSISTANCE GRANTS

Finding Number SA-02-20: Lack of Formal Accounting Records to Support Federal Financial Reports ...(Concluded):

Effect:

Failure to maintain adequate accounting records may result in transactions not being accounted for, in the recording of unauthorized transactions, the unauthorized use or disposition of program assets or in the preparation of inaccurate or incomplete federal financial reports. Therefore, any amounts not used in accordance with program guidelines, or any unauthorized disposition of assets may result in cost disallowances. Furthermore, failure to compare actual expenditures with approved budget at the account level may result in cost disallowances for exceeding approved budgets.

Questioned Costs:

None.

Recommendation:

The Municipality must establish a self-balancing set of accounts for the program and require the accurate and complete maintenance of a full set of accounting records to provide proper accountability over program assets, as well as to enhance the internal controls over these assets, and over the preparation of federal financial reports.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

LOAN GUARANTEE ASSISTANCE (LGA) (SECTION 108 HUD)

Finding Number SA-02-21: Amounts Due From General Fund:

Condition:

The Municipality has not reimbursed the federal program for funds transferred in prior years to finance non-federal activities. At June 30, 2002, the amount owed by the Municipality's general fund to the LGA program amounted to \$1,176,001.

Criteria:

24 CFR 570.200 establishes the various eligible activities to be financed with these funds. However, none of the sections under this Title allows the transfer of federal funds to finance non-federal related activities.

Cause:

This situation occurred because the Municipality incurred expenditures in excess of its available resources in the general fund, and transferred funds from the federal program bank accounts to cover the payments for such expenditures. In addition, the Municipality has not been able to fund this transfer and repay the federal fund.

Effect:

The continued occurrence of this condition results in the financing of the general fund activities with federal funds and limits the funds available to perform the activities approved under the federal grant. This exposes the Municipality to cost disallowances for the amounts owed and may also result in the assessment of penalties and interest costs on amounts owed to the federal programs.

Questioned Costs:

None since this amount has been included as a questioned cost in previous years Single Audit reports.

Recommendation:

The general fund must reimburse the federal program the amount owed as soon as possible. In addition, the Municipality should not permit transfers of federal funds to finance activities not approved by the federal grantor and that are not in accordance with the grant agreements.

- 93 -

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

LOAN GUARANTEE ASSISTANCE (LGA) (SECTION 108 HUD)

Finding Number SA-02-22: Noncompliance with Pledge Requirement:

Condition:

The Municipality does not have an effective internal control system over compliance with the pledge requirements of the LGA Program. During our follow-up procedures we noted that the Municipality did not submit the required pledge document to the federal grantor as guarantee for the repayment of the LGA notes for the 1997-98 grant. The Municipality failed to pledge grants approved or grants for which it may become eligible under 24 CFR 570.705. This must be done in order to assure the repayment of debt obligations and other charges incurred such as issuance, underwriting, servicing, and other costs as a condition for receiving loan guarantee assistance.

Criteria:

Per 24 CFR 570.705, the Municipality shall pledge all grants made or for which it may become eligible to ensure the repayment of debt obligations and the charges incurred such as issuance, underwriting, servicing and other cost, and as a condition for receiving loan guarantee assistance.

In addition, section 4(b) of the Contract for Loan Guarantee Assistance between the Municipality and the Secretary of Housing and Urban Development, dated February 1, 1995 requires that the Municipality should submit to the Secretary an opinion from the Municipality's counsel including the pledge of funds pursuant to 24 CFR 570.705.

Cause:

This situation occurred because the Municipality does not have effective internal controls to oversee the preparation and submission of the pledge document, as required by LGA regulations, prior to obtaining and using program funds.

Effect:

The above situation may impair the Municipality's eligibility to obtain future LGA funds, thus exposing the Municipality to diminished federal financial assistance.

Questioned Cost:

None.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

LOAN GUARANTEE ASSISTANCE (LGA) (SECTION 108 HUD)

Finding Number SA-02-22: Noncompliance with Pledge Requirement...(Concluded):

Recommendation:

The Municipality should immediately submit the required pledge document for the 1997-98 grant. In addition, the Municipality should assign the oversight responsibility to an officer responsible for ensuring the preparation of the corresponding pledge documents for submission to the federal grantor before receiving and using the corresponding program grant funds.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

LOAN GUARANTEE ASSISTANCE (LGA) (SECTION 108 HUD)

Finding Number SA-02-23: Failure to Monitor Program-Income Producing Activities:

Condition:

The Municipality does not have internal controls over monitor compliance relating to the income producing activities that are funded with Program grants. In prior years the Municipality received financing for the acquisition of Paseo Tablado La Guancha and 6 fully developed acres in front of it to be used for parking and other uses. Program income was supposed to be received from lessees of kiosks at La Guancha. Although the Municipality was required to pledge and deposit that program income in a separate identifiable custodial account called the "Loan Repayment Account", we are unable to determine the uses of this rent income, and no income was pledged and deposited for loan repayment purposes.

Criteria:

The 24 CFR 570, and 504 and 24 CFR Part 85, Sections 85.20 (b)(1)(2) and 85.21 (f), require that the grantee must establish the necessary controls for identifying income-producing activities, recording and using program income in accordance with applicable grant agreements and regulations. This is also required in the LGA loan agreement between the Municipality and HUD.

Cause:

This situation has occurred because the Municipality has not established internal controls over compliance with the monitoring of the program-income producing activities to ensure that rent collections are deposited in a separate account to be used for the repayment of the loan. Also, the Municipality has failed to establish internal controls over financial reporting to ensure that these activities are properly accounted for and recorded in the Municipality's accounting records, as required by federal regulation.

Effect:

The continued failure to use program income to pay the LGA loan may allow for funds to be used in ineligible activities to pass undetected, thus exposing the Municipality to cost disallowances for the amounts transferred as well as for program income collected and not used in eligible activities. In addition, the failure to use program income to repay the corresponding loan places an additional limitation in future funding from CDBG, which is the fund that is usually used to repay this loan, because the program income should result in the reduction of the debt service requirement for the corresponding loan.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

LOAN GUARANTEE ASSISTANCE (LGA) (SECTION 108 HUD)

**Finding Number SA-02-23: Failure to Monitor Program-Income Producing Activities
...(Concluded):**

Questioned Costs:

None.

Recommendation:

The Municipality should establish the necessary procedures and ensure that such funds are being deposited in a separate bank account. Furthermore, the Finance Director should be responsible for ensuring that these funds are only to be used for the repayment of the related LGA loan.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

WELFARE-TO-WORK GRANTS TO STATES AND LOCALITIES ("WtW") (CFDA # 17.253)

PROGRAM DESCRIPTION

The objective of the Welfare-to-Work (WtW) grants to States and local communities is to provide funds for transitional employment assistance to move hard-to-employ Temporary Assistance Needy Families ("TANF") recipients with significant employment barriers and certain non-custodial parents into unsubsidized jobs offering long-term employment opportunities. These grants are intended to provide welfare recipients with job placement services, transition employment, and job retention and support services to achieve the ultimate goal of long-term unsubsidized employment and economic self-sufficiency. Funds may be used to help move eligible individuals into jobs by: (1) job creation through public or private sector wage subsidies; (2) on-the-job training; contracts with public or private providers of job readiness, job placement, and post-employment services; (3) job vouchers for similar services; (4) community service or work experience; (5) or job retention and supportive services (if such services are not otherwise available).

At least half of the funds distributed by formula to local areas must be based on a Service Delivery Area's proportion of the State population in high poverty areas. Not more than half may be distributed based on two additional factors: (1) the number of adults receiving TANF assistance for 30 months or more and (2) the number of unemployed in the SDA.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the Welfare-to-Work financial assistance program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

WELFARE-TO-WORK PROGRAM

Finding Number SA-02-24: Inadequate Cash Management Procedures (Prior Report Finding Number SA-01-19) (First Reported 2001):

Condition:

The Municipality's internal controls relating to compliance with the cash management requirements of the federal program are not effective since they are not minimizing the time elapsed between the receipt of funds and its final disbursement for payment.

Criteria:

The Welfare to Work Fiscal and Cash Management Guide issued by the Council establishes that the Program's cash on hand balance shall not exceed a 5-day need.

Cause:

The above exception occurred because the Program's cash requisitions are made to cover the total disbursements for the month and not for its immediate needs. The Program has adopted this approach due to the delay of the Technological Occupational Education Council (the "Council") in disbursing the funds requested by the Program.

Effect:

The continued occurrence of this condition may expose the Municipality to the assessment of interest costs relating to the excess cash on hand, which could be paid from local funds.

Questioned Costs:

None.

Recommendation:

The Municipality should modify the cash forecasting process by establishing a system to forecast the cash needs for the next five days, as established by the Welfare to Work regulations. Federal funds should only be requested when they are going to be disbursed immediately after receipt or within the next five business days.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

HIV CLUSTER - HIV EMERGENCY RELIEF PROJECT AND FORMULA GRANTS (RYAN WHITE) (CFDA #93.914 and #93.915)

PROGRAM DESCRIPTION

The objective of the HIV Emergency Relief Project and Formula Grant Program (Ryan White) is to provide emergency financial assistance to localities that are disproportionately affected by the Human Immunodeficiency Virus (HIV) epidemic to develop, organize and operate programs that provide an effective, appropriate and cost-efficient system for the delivery of essential services to individuals and families with HIV disease.

Funds received under a grant are to be used to provide direct financial assistance for the purpose of delivering or enhancing HIV - related outpatient and ambulatory health and support services, including case management and comprehensive treatment services, for individuals and families with HIV disease; and inpatient case management services that prevent unnecessary hospitalization or that expedite discharge, as medically appropriate, from inpatient facilities.

The Program priorities are the following:

Primary Medical Care - Medication Treatments: this service is expected to increase the availability of medication treatments to the existing HIV/AIDS population. It consists mainly of providing medications, primarily retroviral, to HIV patients.

Home Care: provide care to patients in a home environment.

Laboratory/Diagnostic Services: aimed to provide identified HIV patients with follow-up laboratory procedures and tests. It is intended to expand the availability of lab tests to patients in order to facilitate the delivery of adequate medication.

Home Delivery Meals: a supplemental feeding program that will help the patients to maintain an appropriate level of nutrition by offering daily home delivered meals.

Case Management: maximize the utilization of trained personnel who will take a meaningful interest in the progress of the patient and who will continually aid the patient and family members in scheduling and receiving services, in making adjustments to daily life, and in facing the uncertainties of the disease with a considerable amount of personal support from knowledgeable professionals.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

Transportation: consists of providing transportation services to patients.

The following findings and recommendations arise from our tests of compliance and internal control over compliance requirements applicable to the Ryan White federal financial assistance program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

**HIV EMERGENCY RELIEF PROJECT AND FORMULA GRANTS
(RYAN WHITE)**

Finding Number SA-02-25: Lack of Formal Accounting Records to Support Federal Financial Reports (Prior Single Audit Finding Number SA-01-26) (First Reported 1999):

Condition:

The Municipality does not maintain a self-balancing set of accounts or any type of formal accounting records to account for the transactions and payments of the Program.

The Program does not maintain a formal set of books and accounts. Instead, spreadsheet-based records support accounting and reporting. Therefore, the Program does not have current accurate and complete information with regards to the programs' assets, liabilities, obligations, or unobligated balances, nor is there proper accountability and internal control at program level for the assets owned by the Program. In addition, there is no accurate comparison of actual expenditures against budgeted amounts at the account level.

Criteria:

The 45 CFR Section 92.20(b)(2) establishes that grantees and subgrantees must maintain records that 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. Furthermore, Section 20(b)(3) establishes that effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets. Also, Section 20(b)(4) establishes that actual expenditures or outlays must be compared with budgeted amounts for each grant or subgrant.

Cause:

This has occurred because the Municipality has exercised inadequate oversight over the accounting functions of this Program by not requiring the establishment of a separate set of books for this Program. Instead, the Municipality has permitted the maintenance of informal accounting records, such as spreadsheets, to support the accountability of a major federal program.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

**HIV EMERGENCY RELIEF PROJECT AND FORMULA GRANTS
(RYAN WHITE)**

Finding Number SA-02-25: Lack of Formal Accounting Records to Support Federal Financial Reports (Prior Single Audit Finding Number SA-01-26) (First Reported 1999)...(Concluded):

Effect:

Failure to maintain adequate accounting records may result in transactions not being accounted for, in the recording of unauthorized transactions, the unauthorized use or disposition of program assets or in the preparation of inaccurate or incomplete federal financial reports. Therefore, any amounts not used in accordance with program guidelines, or any unauthorized disposition of assets may result in cost disallowances. Furthermore, failure to compare actual expenditures with approved budget at the account level may result in cost disallowances for exceeding approved budgets.

Questioned Costs:

None.

Recommendation:

The Municipality must establish a self-balancing set of accounts for the program and require the accurate and complete maintenance of a full set of accounting records to provide proper accountability over program assets, as well as to enhance the internal controls over these assets, and over the preparation of federal financial reports.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

**HIV EMERGENCY RELIEF PROJECT AND FORMULA GRANTS
(RYAN WHITE)**

Finding Number SA-02-26: Ineffective Monitoring Procedures (Prior Report Finding Number SA-01-27) (First Reported 1999):

Condition:

The Municipality's internal controls over the monitoring of subrecipients are not designed effectively to monitor activity in order to detect or prevent the payment for services provided to ineligible participants or for ineligible services.

Criteria:

The 45 CFR Section 92.40(a) establishes that grantees are responsible for managing the day-to-day operations of grant and subgrant supported activities. Grantees must monitor grant and subgrant supported activities to assure compliance with applicable Federal requirements and that performance goals are being achieved. Grantee monitoring must cover each program, function, or activity. We believe that the above condition does not provide adequate assurance that the Municipality's monitoring activities are effective.

Cause:

The above situation represents a weakness in the internal control over compliance with the monitoring activities over the service providers. This is because the service providers are responsible for determining eligibility and, since March 1999, the Municipality is not verifying each invoice to determine that the types of services provided as well as the eligibility of these individuals is accurate. Furthermore, since February 1999 the Program's caseworkers became employees of the service providers.

Effect:

Only one person who has no medical or related academic background, which increases the possibility of payments for unallowable services or ineligible participants, performs the Municipality's review.

Questioned Costs:

None.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

**HIV EMERGENCY RELIEF PROJECT AND FORMULA GRANTS
(RYAN WHITE)**

Finding Number SA-02-26: Ineffective Monitoring Procedures (Prior Report Finding Number SA-01-27) (First Reported 1999)...(Concluded):

Recommendation:

The Municipality should hire personnel with academic background and experience in health care to perform periodic monitoring of the activities carried-out by the service providers, and to review and approve medical services invoices.

COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF PONCE

PROGRAMS AUDITED AS MAJOR IN PRIOR YEARS

FINDINGS NOT REPEATED FROM PRIOR AUDIT

- Finding Number SA-01-27 – Funds Disbursed after Period of Availability – Our audit procedures for the current year did not indicate lack of compliance.
- Finding Number SA-01-29 – Noncompliance with Non-Supplanting Requirements – Program was closed during the year.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE

PART VII

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

- 107 -

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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2002**

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-Through Grantor's Number	Expenditures
U.S. DEPARTMENT OF AGRICULTURE - PASS THROUGH COMMONWEALTH OF PUERTO RICO DEPARTMENT OF EDUCATION - Child and Adult Care Food Program	10.558	CCC-049	\$ <u>539,568</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT			
DIRECT PROGRAMS:			
Community Development Block Grant (CDBG)- Entitlement:			
CDBG 01	14.218		5,981,982
CDBG 00	14.218		586,019
CDBG 99	14.218		109,045
CDBG 98	14.218		33,327
CDBG 97	14.218		2,405
CDBG 96	14.218		76,019
CDBG 95	14.218		72,262
CDBG 93	14.218		218
CDBG 92	14.218		9,382
HUD Disaster Recovery Initiative	14.218		1,592,983
Loan Guarantee Assistance	14.248		329,118
Urban Development Action Grant	14.221		39,613
Emergency Shelter	14.231		234,263
Home Ownership Partnership Investment	14.239		381,128
Section 8 - Tenant-Based Cluster:			
Section 8 Rental Voucher Program	14.855		6,038,767
Section 8 - Project-Based Cluster:			
Lower Income Housing Assistance Program - Section 8 - Moderate Rehabilitation I	14.856		727,677
Lower Income Housing Assistance Program - Section 8 - Moderate Rehabilitation II	14.856		<u>433,824</u>
 Total U.S. Department of Housing and Urban Development			 <u>16,648,032</u>
U.S. DEPARTMENT OF LABOR - PASS THROUGH COMMONWEALTH OF PUERTO RICO DEPARTMENT OF LABOR (EMPLOYMENT AND TRAINING ADMINISTRATION):			
Welfare to Work	17.253	Not Available	50,636
Workforce Investment Act Cluster	17.258, 17.259, and 17.260	Not Available	<u>10,600,565</u>
 Total U.S. Department of Labor			 <u>10,651,201</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES			
DIRECT PROGRAMS:			
Administration for Children, Youth and Families - Head Start	93.600		13,007,334
HIV Cluster: HIV Emergency Relief Project and Formula Grants	93.914		<u>1,643,589</u>
 Total U.S. Department of Health and Human Services			 <u>14,650,923</u>
 TOTAL EXPENDITURES OF FEDERAL AWARDS			 <u>\$42,489,724</u>

See notes to Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE**

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2002**

- A. **Basis of Presentation** - The accompanying schedule of expenditures of federal awards is presented on the modified accrual basis of accounting and was prepared primarily from the Municipality's internal accounting records. The financial statements of the Municipality are presented on the basis of governmental activities and funds. The operation of each fund is presented in a separate set of self-balancing accounts that comprises its assets, liabilities, fund equity, revenues and expenditures or expenses, as appropriate. Government resources are allocated to and accounted for by individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The accounts and other accounting records of the Municipality were not designed to capture the information required to prepare the basic financial statements, consequently, such information was obtained from different individuals, departments and accounting records or reports which are not integrated into a double entry bookkeeping system. In addition, several departments within the Municipality are responsible for managing federal financial assistance and there is no centralized control for all federal financial assistance programs.
- B. **Catalog of Federal Domestic Assistance ("CFDA")** numbers are presented for programs for which such numbers are available.
- C. **Reporting Entity** - The Municipality, for purposes of the supplementary Schedule of Expenditure of Federal Awards, includes all the funds of the primary government as defined by GASB Statement 14, *The Financial Reporting Entity*. It does not include any component units of the Municipality as follows:

Corporación para el Desarrollo Económico de Proyectos Comerciales y de Vivienda de
Ponce, C.D. (CODEPCOVI)
Port of Ponce

CODEPCOVI also received federal financial assistance, but separately satisfied the audit requirements of OMB Circular A-133. The Port of Ponce did not receive federal financial assistance during the year ended June 30, 2002.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE**

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2002**

D. Subrecipients

Of the federal expenditures presented, the Municipality provided federal awards to subrecipient as follows:

<u>Program Title</u>	<u>Federal CFDA No.</u>	<u>Subrecipients</u>	<u>Amount Provided</u>
Home Ownership Investment Partnership	14.239	CODEPCOVI	\$ 112,500

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE

PART VII

**CORRECTIVE ACTION PLANS ON
CURRENT YEAR FINDINGS**

- 111 -

ORTIZ, RODRIGUEZ, RIVERA & CO.

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

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ESTADO LIBRE ASOCIADO DE PUERTO RICO
Gobierno Municipal Autónomo de Ponce
SECRETARÍA DE FINANZAS Y TESORERÍA
APARTADO 331709
PONCE, PUERTO RICO 00733-1709

Responses to Findings on Compliance and on Internal Control
Over Financial Reporting Based on the Audit of the Basic
Financial Statements-Year ended June 30, 2002

Finding 02-01: Operating Deficit of General Fund

In recent years, management has implemented several measures and undertaken certain projects to significantly improve its financial position. As result of these, during the fiscal year ended June 30, 2002 the total revenues of the general fund increase by approximately \$19 million. The results of operations shown in the financial statements are mainly affected by the Capital outlays incurred during the year and for which loans from the Government Development Bank had been obtained in prior years. However, management is aware that the results of operations are still showing an operating deficiency because expenditures exceed revenues (prior to other financing sources) and accordingly, it has continued with the implementation of several measures and projects to be able to reach the breakeven point. The most important measures and projects implemented are disclosed as follows:

- a) The Municipality, in coordination with the CRIM has implemented two projects oriented to obtaining additional property tax revenues. The first of these projects was started in late 1998 by the CRIM and it relates to a pilot project initially involving certain municipalities (including Ponce) and consisting of intensified collection efforts on the most recent real property tax accounts receivable, the assessment of real property and the revocation of improper homestead exoneration. This pilot project was approved by the CRIM's Board of Directors and was carried on until January 2000 by a joint effort of CRIM's personnel and outside consultants and appraisers. During November 1999, the CRIM informed the Municipality that through October 31, 1999 a total of 1,368 improper homestead exoneration have been identified as part of the pilot project, resulting in an assessment of approximately \$3 million and that a total of 409 real property assessment has been completed, which amount to \$906,000 in additional taxes. The additional property taxes resulting from this project were expected to be collected during fiscal year 2000-2001 and from the most part represent recurring revenues.

b) The second project was started in 1999 by the Municipality, with the main objective of detecting deficiencies and evasion in the filing of the annual personal property tax returns. As part of the initial phase of this project, the Municipality conducted an economic study and, principally using the municipal license tax roll, determined that for fiscal years 1995-96 through 1997-98, the tax evasion and deficiencies on the self-assessed personal property tax filings amounted to approximately \$21 million for those years. In March 1999, the study was presented to the CRIM's Board of Directors, which granted approval for the Municipality to obtain from the CRIM all the necessary information to carry on the project. On December 8, 1999 the Municipality made a presentation to the Board of Directors of the CRIM to discuss the status of this project. A matching between the CRIM's tax roll of personal property tax filings and the municipal license tax filings has already been made resulting in the identification of specific potential personal property tax evaders. Management has divided the city in eight (8) regions and has commenced to visit the potential evaders to require the filing of the returns for the last four fiscal years. Along with this, collection efforts are being made on the past due real and personal property tax receivables which as per CRIM quarterly report as of September 30, 2002 are approximately \$73 million and \$31 million respectively. During the fiscal year 2002-2003, the CRIM increase the estimated in advances of property taxes for approximately \$275,000 as result of the increase in the collections of past due real and personal property tax receivable.

The second phase of the project consists of the identification of deficiencies in the personal property tax returns filed and was commenced during fiscal year 1999-2000 and, through November 2001, deficiencies amounting to approximately \$2.5 million have been detected. The Municipality has estimated in approximately \$17 million the deficiencies in the filing of the personal property tax returns during the last four years and errors in the filing of returns of \$2.0 million due to taxpayers not segregating in the tax return the personal property located at Ponce. Also, the Municipality has identified approximately \$4.4 million of property tax collections during fiscal year 1995-96 through 1997-98, not credited to the Municipality as part of the annual settlements of advances vs. collections, for which the CRIM is yet to provide an explanation.

All these claims, estimated deficiencies and collections to date by Municipal personnel were presented to and discussed with the CRIM's new administration, which took over in January 2001. The CRIM's new management ordered a special audit of the annual settlements of property tax advances vs. actual collections for the last five (5) fiscal years and stated that most of the Municipality's claims will be investigated as part of that audit. Management believes that the special audit will result in substantial collections not credited to the Municipality which would reduce or eliminate the outstanding debt to CRIM, as result of the aforementioned settlements in recent years. Also, that on a prospective basis, the correction of the problems to be identified through the special audit, should mean additional property tax revenues to the Municipality.

The property tax revenues during fiscal year 2001-02 showed an increase of approximately \$ 521,000, as compared to the prior year, before considering the potential additional revenues discussed above.

- b) In order to increase its financing capabilities with the Government Development Bank for Puerto Rico (the "Bank"), on January 16, 1997 and through Ordinance 99, the Municipality increased from 1.25% to 1.50% the ad-valorem portion of the property tax rates which is restricted for debt service. This increase became effective during the fiscal year 1997-98 and increased such rates to 6.53% and 8.53% for personal and real property, respectively. Due in part to the effect of these rate increases, in April 1999 a loan for \$17.7 million and in June 2001 a loan of \$31.7 million, were obtained from the Government Development Bank. The first of these loans was substantially used to pay accounts payable to suppliers recorded in the general fund as of June 30, 1998. The second loan will be used for capital projects. These loans are being paid through the ad-valorem tax restricted for debt service and therefore, will not require the use of operating funds.

Management estimates that due to the recurring effect of the above mentioned increase of the ad-valorem tax and the anticipated increase in such tax as result of the additional property tax revenues to be generated by the projects described above, the Municipality will be able to obtain loans from the Bank during the near future should there be any significant debt to suppliers in arrears in the general fund as a result of operating deficiencies. The ability of the Municipality to increase its borrowing capacity with the bank in a short period of time was proved by the fact that as of June 30, 2000 it was about \$8 million and one year later (June 2001), the Municipality was able to obtain a loan of \$31.7 million.

- c) As per agreement with the administrator of the Municipal landfill the revenues related to royalties be recognized in future years and rent will be use to pay the current account payable of disposition expenses.
- d) In December 28, 2001, and February 13, 2002 the Municipality received \$9 millions, as advance of the settlement with the Central Government, the total amount for these case is over \$50 millions. Such litigation included matters such as deficiencies in the payments due from several agencies related to the delegation of certain powers and duties to the Municipality, and damages awarded to the Municipality in connection with the Central Government discontinuing the construction of about 54 projects included in the Municipal Land Use Plan. When collected, these revenues will represent an additional financial source, which will mitigate the negative effect of any operating deficiency. Also, the Municipality collected the claim with PREPA related to over-billings in September 2001. The amount settled and collected from PREPA regarding such over-billings was \$2.8 million.

e) In order to achieve its budget control and cost reduction objective, management has established the following measures, among others:

- Managing the Municipality within its cash and budget constraints, including the weekly review and update of its cash flow projections, actual vs. budget comparisons, and the monitoring of the execution of the property tax related projects described above.
- Establishing an immediate short-term cost reduction and cash generating program that systematically identifies and addresses the largest, most effective opportunities for cost reductions and increase in revenues. In connection with this, the Mayor has issued an executive order establishing specific procedures that must be followed by each Department regarding the acquisition of goods and services, in addition to those required by laws and regulations. Before the final issuance of the purchase orders, a division of the Finance Department passes judgment as to the priority, timing and quantity of items being ordered.
- A detailed review of the payroll paid by the general fund was performed in September 1999, which resulted in the identification of certain officers and staff who work directly in the administration of the several federal programs funded by Federal awards, but which payroll costs, payroll taxes and fringe benefits are being paid by the general fund. Such personnel costs have not been included in the grant requests for some of these programs in recent fiscal years, even though the related payroll costs represent allowable costs under the programs. Therefore, starting with the grant requests made during fiscal year 2000-2001, the payroll costs of this personnel have been included as part of the program costs to be funded by Federal awards, so the general fund can experience a reduction in payroll costs.
- As result of the above-mentioned control measures and strategies, as previously mentions total revenues during fiscal years 2001-02 increase by approximately \$19 million, mainly due to increases in property and municipal license taxes. Even though the deficiency of revenues over expenditures remained at the \$9 million, a reduction of approximately \$8.6 million was achieved. However, this decrease was offset by the following factors:
 - Public safety expenditures increased by \$2,574,129 due to certain payroll costs of the police force which prior to this year had been subsidized by COPS and WIA Grants. As result of this, the police force was not reduced but instead, the general fund assumed the total payroll cost.
 - Public works increased by \$2,135,359 million mainly due to required infrastructure maintenance and improvements, in addition to those originally budgeted.

- Capital outlays increased by \$3,421,942 million due to construction projects which started or reached their peak during the year and for which loans from the Government Development Bank had been obtained in prior years, but the related expenditures took place during 2000-01. The fact that there were significant capital projects in process at the beginning of the year is supported by the reserve for capital projects of \$38.4 million shown in the combined balance sheet at June 30, 2001.

Responsibility: Mrs. Myrna Ortiz (Finance Director)
Mrs. Camille Rivera (Budget Director)
Mr. Carlos Jirau, Esq. (City Manager)

Timetable: During the year 2003-2004

Finding 02-02: Expenditures Quarterly Reports Not Submitted

The proper corrective action has been implemented by the management and regarding the budget for fiscal year 2002-2003, estimated of expenditures were submitted by all departments.

Finding 02-03: Inadequate Accounting Practices and Policies

The municipality continues implementing procedures to improve the computerized accounting system, including establishing interface with subsidiary records, integration of the activity of the Federal funds, double entry accounting for all transactions and issuance of a complete General Ledger. Since January 2000, management has been able to produce interim financial information in accordance with generally accepted accounting principles for the General Fund. This information has helped management to analyze results of operations and prepare cash flow projections and consequently, to better manage its operational budget. Therefore, the continuing development of its accounting system is allowing the Finance Department to implement the appropriate corrective actions to resolve this situation and comply with the applicable Article 8.010 of the Municipal Autonomous Law and with the auditor's recommendations.

Responsibility: Mrs. Myrna Ortiz (Finance Director)
Mrs. Camille Rivera (Budget Director)
Mr. Carlos Jirau (City Manager)

Timetable: Fiscal year 2003-2004.

Finding 02-04: Inadequate Accounting for Interfund Transactions

As mentioned in the response to the previous finding, the Municipality is enhancing its computerized accounting system and as part of this, a subsidiary ledger will be established to properly account for inter-fund transactions.

However, the practice of transferring Federal funds to finance operations of the General Fund has been discontinued in past years, following an executive order by the Mayor. The debt by the General Fund to the Head Start Program was fully repaid as of the end of fiscal year 1998-99 and payments continue to be made to LGA. Regarding the debt from General Fund to the CDBG Programs, the financial consultants of the municipality verified in detail all transactions related to these outstanding debt and determine that it was an accounting errors carried over from prior years.

Responsibility: Mrs. Myrna Ortiz (Finance Director)

Timetable: Fiscal year 2003-2004 or shortly thereafter.

Finding 02-05 Inactive and Unnecessary Fund and Account are not Closed (Prior Report Finding Number 00-09) (First Reported 1986):

The situation describe was fully corrected during 2002-2003.

Finding 02-06: Checks outstanding in Excess of Six Months

Checks will be investigated and will be cancelled. As part of the monthly bank reconciliations procedures, instructions will be given to cancel all checks outstanding over six months.

Responsibility: Mr. Myrna Ortiz (Finance Director)
Mrs. Irma Rosado (Finance Deputy-Director)

Timetable: On-going.

Finding 02-07: Construction Excise Tax Files not Available:

The management of the municipality is aware of this situation. The Finance Director will coordinate we the department of Municipal License Tax and the Office of Permits to prepare the corrective action to improve the procedures for the determination of the Excise Taxes.

Responsibility: Mr. Myrna Ortiz (Finance Director)

Timetable: June30, 2003

Finding 02-08: Inadequate Control over Voucher for Payment and Related Documents:

The Finance Director will coordinate with the accounting department to assure this matter will not continue.

Responsibility: Mr. Myrna Ortiz (Finance Director)

Timetable: June 30, 2003

Finding 02-09: Lack of Supporting Documentation for Municipal License Taxes:

The Finance Director required to the financial consultants an evaluation of all files returns to determine all possible errors, lack of supporting documentation and deficiencies in the Volume of Business Declaration of taxable income. Also the Finance Director carryout a meeting with the municipal license tax employees to coordinate the duties of each one and assure correct the instance state in this finding.

Responsibility: Mr. Myrna Ortiz (Finance Director)

Timetable: June 30, 2003

Finding 02-10: Incomplete Documentation in Employees Files:

This matter was corrected during the year 2002-2003

Responsible: Mrs. Ivonne Laborde

Timetable: Fiscal Year 2002 - 2003



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PONCE, PUERTO RICO 00733-1709

Management's Corrective Action Plan
on Findings on Compliance and on Internal Control Over Compliance
with Requirements Applicable to Federal Programs
Fiscal Year ended June 30, 2002

Finding SA-02-01: Lack of Reconciliation Procedures

Currently, the Municipality's Finance Department performs all cash disbursements functions of the Programs. The Municipality has assigned personnel to reconcile the Programs' bank accounts and send copies to the various Programs on a timely basis, to ensure recording in the Programs' books of all cash transactions. Also, some of the programs have assigned personnel to assist the Municipality in the reconciliation and cash disbursement procedures. With these measures the Municipality is verifying that transactions recorded at the Municipality's accounting department are also recorded in the Programs' accounting records.

In addition, as part of the enhancement being made to the computerized accounting system, the accounting information maintained at the Programs will be integrated into that system's General Ledger in the corresponding fund. This will allow for a closer monitoring of the transactions related to the Federal Programs and for a centralized accounting system which include all fund types.

Responsibility: City Manager, Finance Director and Programs' accountants

Timetable: Fiscal years 2002-2003.

Finding Number SA-02-02: Amounts Due from General Fund (Prior Report Finding Number 01-02) (First Reported 1988):

Upon further review of these amounts and assistance received from our financial consultants, we have determined that most likely, the \$392,133 relates to intrafund balance among the various programs under the Municipality's Department of Economic and Community Development (DEC, in it Spanish acronym), and not to amounts withdrawn by the General Fund from DEC. During recent years, several expenditures have been shared by different programs under DEC, whereby one program paid in full for other programs, thus creating intrafund balances. Such balances were apparently not properly accounted for when the Special Revenue fund was consolidated, for

purpose of the presentation of the Municipality's Basic Financial Statements. This caused the external auditors to propose, and the Municipality recorded, an adjustment attributing the intrafund balance to General Fund, as if Federal Fund had been transferred to this. Further analysis is need to corroborate this situation and be able to identify the specific intrafund balances that amount to \$392,113 and properly adjust this balance as part of the next year-end closing.

Regarding the remaining \$724,188, the amount resulted from an audit adjustment recorded in fiscal year 1992-93 because of an incorrect debit balance in the deferred revenue account. Management initially determined that this amount resulted from funds transferred to General Fund and recorded in the Program's books a receivable from such Fund. However, a further analysis of the activities for grant years 1985 through 1994 indicated that there were no expenditures in excess of the line of credits, except for 1989 and 1993, which excess amount to only \$76,303, combined. Therefore, we believe that the unidentified amount of \$647,885 (\$724,199 less \$76,303) relates to accounting errors and we are waiting for its final determination to proceed accordingly.

Responsibility: Mr. Alex Lopez, PE (Program Director)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: Will depend on when the Grantor agency reach a final determination.

Finding SA-02-03: Financial Summary Report is Inaccurate

Difference is being investigated and has already been partially adjusted.

Responsibility: Mr. Osvaldo Maldonado (Contador IV)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: Fiscal year 2002-2003

Finding SA-02-04: Inadequate Cash Management Procedures

The corrective actions described in our response to Finding SA-02-01, have significantly improved the Program's cash forecasting procedures and minimized the occurrence of events of non-compliance regarding the applicable cash management requirements. Such actions include assigning a staff of the Program to assist the Finance Department of the Municipality to accelerate the disbursement process and monitor the requests of funds which are not made until the Municipality has completed the required approval procedures of the disbursements and is ready to issue the checks. Most of the exceptions noted by the auditors relate to disbursements made one additional day to the three-day requirement.

Responsibility: Mr. Osvaldo Maldonado (Contador IV)
Mr. Myrna Ortiz (Finance Director)

Timetable: Continuously.

Finding SA-02-05: Unliquidated Obligations of Closed Program Years not credited to Federal Program

This amount is the result of the invoice prepared by the supplier by a \$1 short. It will be adjusted to be eliminated. The \$23,480 correspond to the retained of 10%. The management will investigate this situation for the proper accounting treatment.

Responsibility: Mr. Osvaldo Maldonado (Contador IV)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: Fiscal year 2002-2003.

Finding SA-02-06 Failure to Monitor Program-Income Producing Activities

During the first semester of fiscal year 2002-03, an evaluation of the program income activities was performed by the financial consultants. Since the second semester Director of Finance's staff will be giving monitoring to the activities of them mentioned programs-income and they developed an annual work plan so that the funds are used accordance with the applicable grant provisions and regulations.

Responsibility: Mr. Myrna Ortiz (Finance Director)
Mr. Carlos Jirau (City Manager)

Timetable: Fiscal year 2002-2003

Finding Number SA-02-07: Interest Earned Not Remitted to Federal Grantor (First Reported 1987):

This amount was reimbursed to the Federal Grantor on November 12, 2002 through the payment voucher # 03-25-0142.

Finding SA-02-08: Inadequate Cash Management Procedures

The average balance on hand significantly exceeded the average cash need of the programs because many participants have to return money for which is not eligible. The participants abandon the program or change his economic income status. This situation cause less disbursement by the program. Related to interest income these are reducing from the total expenditure of the sub-program Voucher upon finalizing the fiscal year. This is the reason for which the program does not have return the interest to the Grantor.

Responsibility: Mr. Alex López, Esq. (Program Director)
Mrs. Myrna Vales (Program Deputy Director)
Mr. Myrna Ortiz (Finance Director)

Timetable: Fiscal year 2002-03 and continuously.

Finding Number SA-02-09 Amounts Due From General Fund (Prior Report Finding Number 00-11) (First Reported 1992):

The Municipality of Ponce is carrying out an investigation to determine if the \$1,268,349 is not an accounting error. Further transactions are being investigated to be able to determine the correct balance of debt if any.

Finding SA-02-10: Inadequate Documentation of Participant files

The information was available at the Program, but at the time of the audit those information were not included in the participant's file. In addition, the Municipality has an internal auditor assigned to perform tests of compliance at several Federal Programs. Such tests include the verification of completeness of the participants' files.

Responsibility: Mrs. Lizette Caballero (Program Supervisor)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: On-going

Finding SA-02-11: Inadequate Cash Management Procedures

To improve cash management procedures, the Program is delaying the request of Funds to the Grantor until the approved disbursement vouchers have been delivered to the Municipality's Finance Department for the processing of the checks. However, the workload at the Finance

Department is causing delays in the approval and check issuance procedures. Accordingly, to keep improving cash management procedures, the Program is waiting until the checks are received from the Finance Department, prior to making the funds requests. This should help prevent instances of noncompliance with regards to the time elapsing between the receipts of funds and their disbursements.

Responsibility: Mr. Alex López, Esq. (Program Director)
Mrs. Myrna Vales (Program Deputy Director)
Mrs. Myrna Ortiz (Finance Director)
Mr. Osvaldo Maldonado (Contador IV)

Timetable: Fiscal year 2002-2003

Finding SA-02-12 Noncompliance with the Period of Availability of Federal Funds

This program requires that the funds should be assign within the period of two years. Parts of those funds were assigned within the period required by the grantor. However, many of the materials for the betterments or constructions of dwelling are assigned as needed, during the constructions. Those constructions or betterments were performed in more than two years, therefore it was impossible to assign all funds before needed.

Responsibility: Mr. Alex López, Esq. (Program Director)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: Fiscal year 2002-2003

Finding SA-02-13: Ineffective Controls Over Preparation and Submission of Federal Financial Reports

When the financial report is prepared and sent to the Federal Grantor some expenditures were not registered in the books. Controls will be enhanced regarding the issuance of financial information to the Grantor agency to prevent this type of discrepancies in the future.

Responsibility: Mr. Alex López, Esq. (Program Director)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: Fiscal year 2002-2003.

Finding SA-02-14: Noncompliance with Earmarking Requirement:

The expenditure for this "Federal Grant" has not been spent completely because the works and improvements to the pluvial system of the "Playa de Ponce" have had problems with the water pump function. For such reason The Department of Engineering of HUD Ponce does not certificate these works.

Responsibility: Mr. Alex López, Esq. (Program Director)
Mrs. Myrna Vales (Program Deputy Director)
Mr. John Serra (Director of The Department of Engineering)

Timetable: Fiscal year 2002-2003.

Finding SA-02-15: Inadequate Cash Management Procedures

The process established by the Grantor of WIA for the petition of fund is oriented for the request of funds in a monthly basis. It is the result of the information is entered to the electronic system, it establishes the budget for the following month and the funds are requested electronically. The Director of the program is preparing a new method for the petition to minimize the time elapsed between the receipt of funds and final disbursement to payment.

Responsibility: Mr. Ramón Anglada (Program Director)
Mrs. Pierrette Rebollar (Program Deputy Director)

Timetable: Fiscal year 2002-2003.

Finding SA-02-16: Ineffective Controls Over Preparation and Submission of Federal Financial Reports (Head Start)

Controls will be enhanced regarding the issuance of financial information to the Grantor agency to prevent this type of discrepancies in the future.

Responsibility: Mr. Wilfredo Rodríguez (Fiscal Officer)
Mrs. Damaris Suliveres (Program Accountant)

Timetable: Fiscal year 2002-2003

Finding SA-02-17: Failure to Meet Full Enrollment Level

The petitions of funds related to the program year 2002 were made based on centers which are in existence. However, some of these centers still need betterments to make them suitable for providing the services kind environment that the Federal regulations require. Currently, there are betterments being performed at Albergue de Niños building which should provide additional participants. As result of these betterments performed to those centers the deficiency in the enrollment of the participants, should be resolved by June 30, 2003.

Responsibility: Mrs. María de los A. Torres (Program Director)
Mr. Wilfredo Rodríguez (Fiscal Officer)

Timetable: Program year 2003.

Finding SA-02-18: Inadequate Cash Management Procedures

The checks referred in this finding are those that they are used to cover the expense of payroll. Controls will be enhanced regarding the issuance of financial information to the Grantor agency to prevent this type of discrepancies in the future.

Responsibility: Mr. Wilfredo Rodríguez (Fiscal Officer)
Mrs. Damaris Suliveres (Program Accountant)

Timetable: Fiscal year 2002-2003

Finding SA-02-19: Failure to Meet the Minimum Required Average Daily Attendance Level

Even though controls exist to deal with this compliance issue, the daily attendance of participants is a recurring problem very difficult to deal with, as it usually relates to family matters and circumstances beyond the control of the Program.

Currently, the social services staff of the Program performs periodic visits to the participants' parents to investigate the causes for absenteeism and provide orientation to minimize this. Also, absence patterns are analyzed to evaluate the reasons for these. These controls will continue to be performed and enhanced until the required attendance levels are met.

Responsibility: Area Managers
Mrs. María de los A. Torres (Program Director)

Timetable: Continuously until the required attendance level is met.

Finding SA-02-20: Lack of Formal Accounting record to Support Federal Financial Report

Procedures will be implemented to establish a set of accounting records and allow the recording of transactions related to the program, in accordance with the applicable regulation.

Responsibility: Mr. José Chompré (Program Accountant)
Mrs. Myrna Ortiz (Director of Finance)
Mr. Carlos Jirau (City Manager)

Timetable: Fiscal Year: 2002-2003

Finding SA-02-21: Amount Due From General Fund

As of January 31, 2003, the Municipality has paid \$200,000 as part of the agreement of paying \$50,000 monthly or a greater amount according to the financial situation of the Municipality of Ponce.

Responsibility: Mrs. Myrna Ortiz (Director of Finance)
Mr. Carlos Jirau (City Manager)

Timetable: Continuously until pay off the debt.

Finding SA-02-22: Noncompliance with Pledge Requirement:

This matter is being handled by Municipality's legal counsels.

Responsibility: Mr. Alex López, Esq. (Program Director)
Mrs. Myrna Vales (Program Deputy Director)

Timetable: Fiscal Year 2002-2003

Finding SA-02-23: Failure to Monitor Program-Income Producing Activities

During the first semester of fiscal year 2002-03, an evaluation of the program income activities was performed by the financial consultants. Since the second semester Director of Finance's staff will be giving monitoring to the activities of them mentioned programs-income and they developed

an annual work plan so that the funds are used accordance with the applicable grant provisions and regulations.

Responsibility: Mr. Myrna Ortiz (Finance Director)
Mr. Carlos Jirau (City Manager)

Timetable: Fiscal year 2002-2003

Finding SA-02-24: Inadequate Cash Management Procedures

To improve cash management procedures, in recent years the Program was delaying the request of Funds to the Grantor until the approved disbursement voucher have been delivered to the Municipality's Finance Department for the processing of the checks. However, the heavy workload at the Finance Department is causing delays in the approval and check issuance procedures. Accordingly, to keep improving cash management procedures, since October 2000 the Program are waiting until the checks are actually received from the Finance Department, prior to making the funds request. This should help prevent instances of noncompliance with regards to the time elapsing between the receipts of funds and their disbursements.

Responsibility: Mr. Ramón Anglada (Program Director)

Timetable: Fiscal year 2002-2003

Finding SA-02-25: Lack of Formal Accounting Records to Support Federal Financial Reports

In the work plan of the program it is contemplated the acquisition of a system automated to improve the accounting system. In the next proposal an increase in the administrative percent of expenses was proposed to cover the system to be acquired and hire a bookkeeper for the program.

Responsibility: Mr. Myrna Ortiz (Finance Director)
Mr. Carlos Jirau (City Manager)
Mr. Luis Cruz (Program Director)

Timetable: Fiscal year 2002-2003

Finding SA-02-26: Ineffective Monitoring Procedures

In coordination with the Director of Internal Auditing of the Municipality of Ponce and the Director of the program agreed to place of permanent form to personnel of that department to

monitor the financial processes and thus to avoid disbursements or transactions not authorized. The Municipality contracted the services of a medical specialist to monitor of the services offered to the patient and another person for the revision and preparation of the medical record of patient. Currently, the Municipality is carrying out a process to acquire personnel in other areas of support.

Responsibility: Mr. Myrna Ortiz (Finance Director)
Mr. Carlos Jirau (City Manager)
Mr. Luis Cruz (Program Administrator)

Timetable: Fiscal year 2002-2003

Municipality of Ponce
Comprehensive Annual Financial Report
June 30, 2002

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Prepared by the Municipality of Ponce

Hon. Rafael Cordero Santiago
Mayor

Carlos Jirau
City Manager

Myrna Ortiz
Finance Director

October 25, 2002



MUNICIPALITY OF PONCE

Comprehensive Annual Financial Report

June 30, 2002

Table of Contents

Part I. Introductory Section	Page
Transmittal Letter	2-7
Organization Chart	8
List of Elected and Appointed Official	9
Part. II Financial Section	
Independent Auditors' Report	11-12
Management Discussion and Analysis	13-22
Basic Financial Statements:	
Statement of Net of Assets	23-24
Statement of Activities	25
Fund Financial Statements:	
Balance Sheet – Governmental Funds	26-27
Reconciliations of the Governmental Funds Balance Sheet to the Statement of Net Assets	28
Statement of Revenues, Expenditures, and Changes in fund Balances	29-30
Reconciliation of the Statement of Revenues, Expenditures and in fund balance to the Statement of activities	31
Statement of Revenues and Expenditures – Budget and Actual – General and Debt Services Funds	32
Notes to the basic Financial Statements	33-66

(Continued)

MUNICIPALITY OF PONCE

Comprehensive Annual Financial Report

June 30, 2002

Table of Contents

	Page
Combining Individual Fund Statements:	
General Fund:	
Comparative Balance Sheets	68
Comparative Statements of Revenues, Expenditures and Changes in Fund Balance	69
Nonmajor Governmental Funds:	
Combining Balances Sheet – Nonmajor Governmental Funds	70
Combining Statement of Revenues, Expenditures, and Changes in Fund Balance – Nonmajor Governmental Funds	71
Capital Assets Used in the Operations of Governmental Funds – Schedule of Changes by Function and Activity	72
 Part III. Statistical Section	
General Governmental Revenues by Source	74
General Governmental Expenditures by Function	75
Assessed Value of Taxable Real and Personal Property	76
Real and Personal Property Tax Levies and Collections	77
Property Tax Rates	78-79
Computation of Legal Debt Margin	80

(Continued)

MUNICIPALITY OF PONCE

Comprehensive Annual Financial Report

June 30, 2002

Table of Contents

	Page
Ratio of General Bonded Debt to Assessed Value and Net Bonded Debt per Governmental Expenditures	81-82
Construction and Bank Deposits for the Last Ten Fiscal Years	83
Comments relative to Statistical Section	84
Demographic Statistics for the Last Ten Years	85

PART I. INTRODUCTORY SECTION



ESTADO LIBRE ASOCIADO DE PUERTO RICO

Gobierno Municipal Autónomo de Ponce

Oficina del Alcalde

Rafael Cordero Santiago
Alcalde

October 25, 2002

To the Honorable Mayor and Member of the Municipality
Assembly and the Residents of the Municipality of Ponce:

State law requires that all general-purpose local governments publish within six months of the close of each fiscal year a complete set of financial statements presented in conformity with general accepted accounting principles (GAAP) and audited in accordance with generally accepted auditing standards by a firm of licensed certified public accountants. Pursuant to that requirement, we hereby issue the comprehensive annual financial report of the Municipality of Ponce for the fiscal year ended June 30, 2002.

This report consists of management's representations concerning the finances of the Municipality of Ponce. Consequently, management assumes full responsibility for the completeness and reliability of all of the information presented in this reports. To provide a responsible basis for making these representations, management of the Municipality of Ponce has established a comprehensive internal control framework that is designed both to protect the government's assets from loss, theft, or misuse and to compile sufficient reliable information for the presentation of the Municipality of Ponce financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the Municipality of Ponce comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert to the best of our knowledge and beliefs, this financial report is complete and reliable in all material respects.

The Municipality of Ponce financial statements have been audited by Ortiz, Rodríguez Rivera & Co. a firm of licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the Municipality of Ponce for the fiscal year ended June 30, 2002, are free of material misstatement. The independent audit involved examining, on a test basis, evidence

supporting the amounts and disclosure in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statements presentations. The independent auditors concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the Municipality of Ponce financial statements for the fiscal year ended June 30, 2002 are fairly presented in conformity with GAAP. The independent auditor's report is presented as the first component of the financial section of the report.

The standards governing Single Audit engagement require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited government's internal control and legal requirements involving the administration of federal awards. These reports are available in the Municipality of Ponce separately issued Single Audit Report.

GAAP require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The Municipality of Ponce's MD&A can be found immediately following the report of the independent auditors.

Profile of the Government

The Municipality of Ponce, incorporated in 1692, is located in the south part of Puerto Rico, one of the top growth areas of the island. The Municipality of Ponce currently occupies a land area of 184.47 square miles and serves a population of 187,935. The Municipality of Ponce is empowered to levy a property tax on both real and personal properties located within its boundaries.

The Municipality of Ponce has operating under the Commonwealth since 1952. Policy-making and legislative authority are vested in a Legislative Assembly consisting of the mayor and sixteen legislative assembly members. The Legislative Assembly is responsible, amount other things, for passing ordinances, and approving the budget and any budget transfer is necessary. The City manager is responsible for carrying out the polices and ordinances of the Legislative Assembly, for overseeing the day-to-day operations of the government. Legislative Assembly members serve for four-years.

The Municipality of Ponce provides a full range of services, including police and fire protection; the construction and maintenance of highways, streets, and other infrastructure; and recreational activities and cultural events. The Municipality of Ponce also is financially accountable for a legally separate Port and a legally Corporation for Housing and Commercial Development (CODEPCOVI), both of which are reported separately within the Municipality of Ponce statements. Additional information on all three of these legally separate entities can be found in Note 2 to the financial statements.

The Annual budget serves as the foundation for the Municipality of Ponce's financial planning and a control. All departments of the Municipality of Ponce are required to submit request for appropriation to the Budget Director on or before of April 30 each year. The Budget Director uses these requests as the starting point for developing a proposed budget. The Budget Director, then present this proposed budget to the Mayor for review prior to May 15. The Mayor is required by the Law 81 to present this budget to the Legislative Assembly no later than May 31. The Legislative Assembly is required to hold public hearings on the proposed budget and adopt a final budget no later than June 13 each year. The appropriated budget is prepared by fund, function, and department. Transfers of appropriations between departments, however, require the special approval of the Legislative Assembly. Budget to actual comparisons are provided in this report for each individual governmental fund for which an appropriated annual budget has been adopted.

Factors Affecting Financial Condition

The information presented in the financial statement is perhaps best understood when it is considered from the broader perspective of the specific environment within which the Municipality of Ponce operates.

Local economy. The Municipality of Ponce currently enjoys a favorable economic environment and local indicators point to continued stability. The region has a varied manufacturing and industrial base that adds to the relative stability of the unemployment's rate.

The Municipality of Ponce has an employed labor force of approximately 56,335, which is anticipated to grow at a rate of between 3 percent and 4 percent each year for the next several years. This expectation is base on the development of the Las Americas Port, during the year 2001-2002 the gross revenues of the Port of Ponce was \$2.3 millions. During the year ended June 30, 2002 the Port of Ponce manage 55,903 containers and 850,030 tons. The export and imports increase a 9 % during this year. The board of Director of the Ponce Port has been working on the engineering studies and has obtained the constructions plans for the improvement of piers 4, 5, 6, and 7A. The Port received 245 ships with 2.9 tons, an increase of 4% vs. prior year. The expectation in the development of the Port of Ponce is to increase the Port operations 10 times, and that increase will benefit the economic of the Municipality of Ponce as a whole.

The government's central business district is expended to maintain its current 97 percent occupancy rate with a variety of store, specially shop, and commercial businesses. Meanwhile, there continues to be a discernable trend toward steady residential growth.

Long-term financial planning. The Municipality of Ponce plan to develop the following projects during the year ended June 30, 2003:

1. Sewer System of Las Americas Avenue	\$ 5,000,000
2. Construction of Public library and Historic Deposit	4,500,000
3. Improvements to Concha Acústica	1,000,000
4. Improvements to Monagas Park	2,500,000
5. Morell Campos Institute	2,500,000
6. Improvements City Hall	8,800,000
7. Bellas Artes Center	20,000,000
8. Improvements to various streets and sectors	<u>11,892,406</u>
Total	<u>\$56,192,406</u>

The administration of the Municipality has design other projects for the next 3 years and has already obtained the commitments from Commonwealth that funding will be available from the general budget. Some of those projects are as follow:

1. Improvements to Santiago de los Caballeros Avenue	\$15,000,000
2. Construction of PR 9 road to PR 123 road	11,179,411
3. Construction of PR to Urb. Jardines del Caribe	17,363,077
4. Improvements to High way PR 2	7,500,000
5. Improvements to Hostos street to Las Americas Ave.	2,000,000
6. Improvements to 14 road	6,000,000
7. Improvements to PR 503 to Mayor Cantera Street	5,000,000
8. Improvements to PR 139 road	5,350,000
9. Improvement to Port of Ponce	400,000,000
10. Channel of Bucaná-Portugués river	103,000,000
11. Others minors constructions	28,500,000
12. Rafael Lopez Nusa -	20,000,000
13. Residencial Caribe -	11,500,000
14. Lirios del Sur -	<u>18,000,000</u>
Totals	<u>\$650,392,488</u>

Other projects will be finance by loans with the Economic Development Bank and the expectations are to be completed by June 30, 2005.

Those projects are as follow:

1. Improvements Pachin Vicens Park	\$8,100,000
2. Francisco Montaner field	5,800,000
3. Improvements to Recreational Park	2,500,000
4. Dredge in the Port	30,000,000
5. Purchase of equipments and improvements to pier 7 & 8	50,000,000
6. Various Basketball field	5,000,000
7. Extension to Lineal Park	<u>5,000,000</u>
Total	<u>\$ 108,900,000</u>

Cash management polices and practices. Cash temporarily idle during the year was invested in certificates of deposit. The maturities of the investment range from 30 to 60 days. The average yield on investments was 2 to 2.5 percent. Investment income for the year ended June 30, 2002 was \$1,899,811.

Risk Management. The Administration of the Municipality of Ponce performed an evaluation of the valuation of all Municipal property looking for obtain an insurance for damage which cover a real amount of value of the properties. All acquisitions or sales of properties are supervised by the Director each of the department, the Municipality performed annual inventory of all personal and real property.

Additional information on the Municipality of Ponce risk management activity can be found in Note j of the notes to the financial statements.

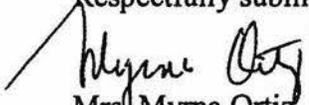
Awards and Acknowledgements

The Comptroller of Puerto Rico awarded a Certificated of Compliance with the Standard for the improvements of the Municipal Administrations to the Municipality of Ponce. This was the second consecutive year that the Municipality of Ponce has received this prestigious award.

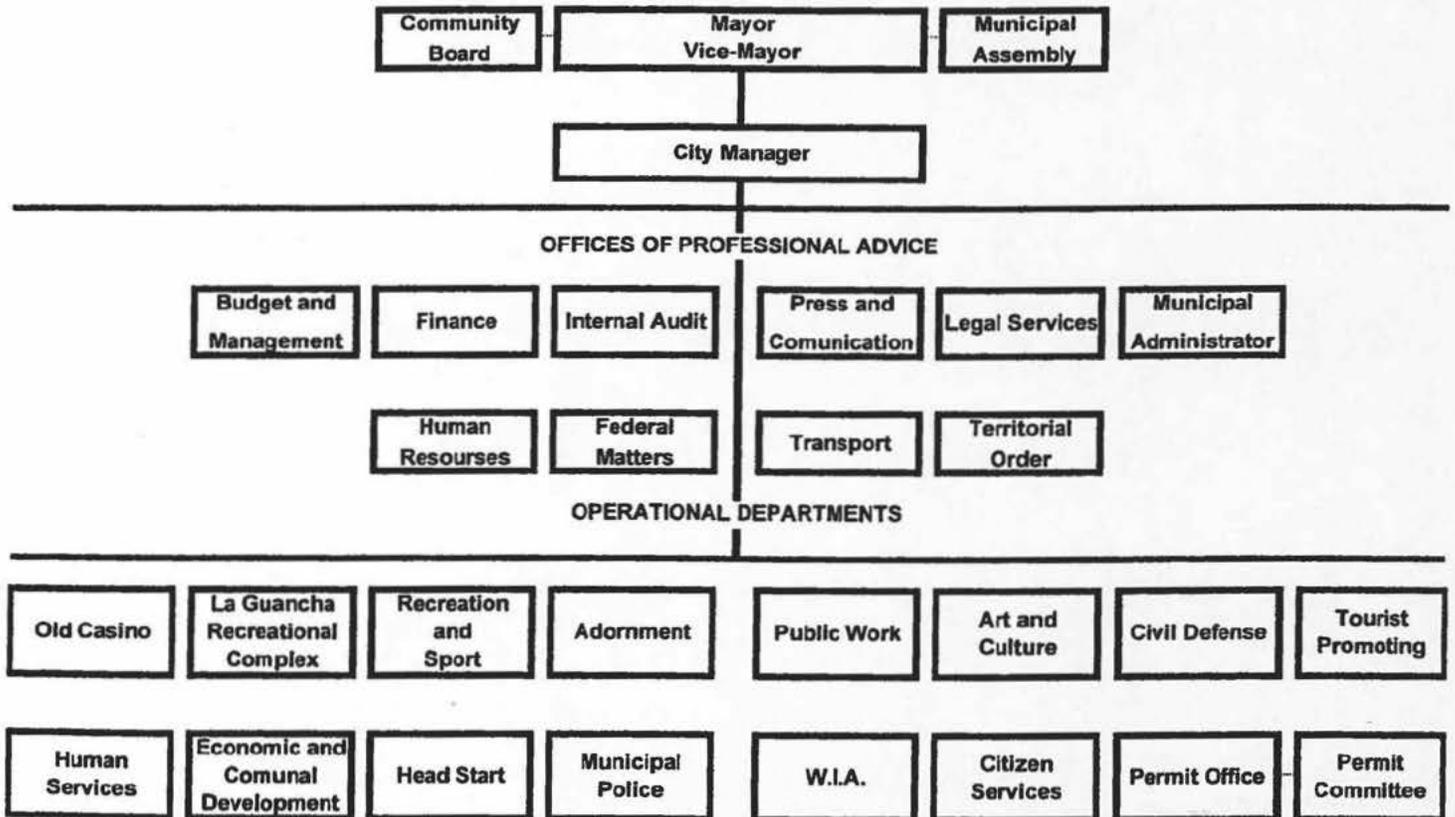
In addition, the Municipality of Ponce received an award from Commonwealth of Puerto Rico for the performance of the standard with the Work Investment Act program.

The presentation of this report would not have been possible without the efficient and dedicated service of the entire staff of the finance and administration department. We would like to express our appreciation to all member of the department who assisted and contributed to the preparation of this report and also we would like to give special thanks to our independent auditors Ortiz, Rodríguez Rivera & Co. for their commitment. Credit also must be given to the Mayor for the professionalism in the management of the Municipality of Ponce finance.

Respectfully submitted,


Mrs. Myrna Ortiz
Finance Director

Municipality of Ponce Organization Chart



Municipality of Ponce

List of Elected and Appointed Officials

Elected Officials

Mayor

Rafael Cordero Santiago

Legislative Municipality Assembly

Luis A. Morales, President
Enrique A. Vicéns, VicePresident
Pedro Pacheco Figueroa
Enrique Amy Fernández
Waldemar Vélez Silvagnoli, Majority Spokesperson
René Garrastazú
Daisy Silvagnoli Maldonado
Simona Santiago Ruiz

CarlosL. Baéz Muñiz
Freddie Martínez Sotomayor
Juan H. Cintrón García
Elioscar Pérez Ramírez
Santos Silva Ojeda
María Cristina Martínez Torres
Ruth García Ortíz
Nilda González González

Appointed Officials

Carlos Jirau
Myrna Ortíz
Camille Rivera
Lilliam Santiago
Mabel Pola
Patricia Castaing
Vilma Flores
Ivonne Laborde
Alex Lopéz
Wilfredo Morales
Minerva Canevaro
Gerardo Tripari
Aby Martínez
Pedro Hernández
Paul Fourquet
Vangie Rivera
José Medina Orta
Maria De los Angeles Torres
Gilberto Rodríguez
Ramón Anglada
Wanda Rodríguez Feria
Juan Carlos Santiago
Miguel Mercado

City Manager
Office of Finance
Office of Budget
Office of Internal Audit
Office of Press
Office of Legal Affair
Office of Municipal Secretary
Human Resources
Department of Economic Development
Department of Ornament
Casino
Office of Recreation Complex
Department of Sport and Recreation
Department
Civil Defense
Turist development
Human Services
Head Start department
Commissioner of Police and Public Safety
Work Investment Act Department
Citizens Services
Historic Center
License and Permits

PART II. FINANCIAL SECTION



ORTIZ, RODRIGUEZ, RIVERA & CO.
CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

CPA Orlando Luis Ortiz Cabrera
CPA Marco Antonio Rivera Zúñiga
CPA Luis O. Rivera Zúñiga

Members:
American Institute of Certified
Public Accountants (AICPA)
Puerto Rico Board of Certified
Public Accountants
Management Consulting
Services Division

INDEPENDENT AUDITORS' REPORT

**To the Honorable Mayor and
Municipal Council
Municipality of Ponce
Ponce, Puerto Rico**

We have audited the accompanying basic financial statements of the Municipality of Ponce, as of and for the year ended June 30, 2002, as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the Corporación para el Desarrollo Económico de Proyectos Comerciales y de Vivienda de Ponce, C. D. ("CODEPCOVI") and of the Port of Ponce which are shown as discretely presented component units. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for CODEPCOVI and the Port of Ponce, is based solely on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit and reports of the other auditors, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Municipality of Ponce as of June 30, 2002, and the results of its operations for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2 to the basic financial statements, the Municipality of Ponce has implemented a new financial reporting model, as required by the provisions of the Governmental Accounting Standards Board ("GASB") Statement No. 34, Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments, as of June 30, 2002

The Management's Discussion and Analysis on pages 13 through 22 is not a required part of the basic financial statements, but is supplementary information required by the GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining and individual nonmajor fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

San Juan, Puerto Rico
October 25, 2002

The stamp 1812093 was affixed
to the original of this report



**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

MANAGEMENT DISCUSSION AND ANALYSIS

Our discussion and analysis of the Municipality of Ponce's financial performance provides an overview of the Municipality's financial activities for the fiscal year ended June 30, 2002. Please read it in conjunction with the transmittal letter on page 2 and the financial statements, which begin on page 11.

FINANCIAL HIGHLIGHTS

- The Municipality's net assets increase as a result of this year's operations. Net assets as of June 30, 2002 are \$151.1 million, as compared to \$ 137.2 million for the year ended June 30, 2001, for a 10% of increase.
- During the year, the Municipality had revenues that were \$ 6.7 million more than the \$82.8 million incurred in expenses for governmental programs. This compares to last year, when revenues exceeded expenses by \$8.6 million.
- The investment in capital assets for this year is \$ 11.4 million.
- Loans principal payments were \$3.9 million, decreasing long-term debt from \$195.8 million in 2001 to \$171.3 million in 2002.
- Resources available for appropriation were \$99.0 million more than budgeted for the General Fund.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Assets and the Statement of Activities (on pages 23 and through 25) provide information about the activities of the Municipality as a whole and present a long-term view of the Municipality's finances. Fund financial statements start on page 26. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the Municipalities' operations in more detail than the government-wide statements by providing information about the Municipality's most significant funds.

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

Reporting the Municipality as a Whole

The Statement of Net Assets and the Statement of Activities

The Statement of Net Assets and the Statement of Activities report information about the Municipality as a whole and about its activities. These statements include *all* assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Municipality's *net assets* and changes in them. You can think of the Municipality's net assets, the difference between assets and liabilities, as one way to measure the Municipality's financial health, or *financial position*. Over time, *increases or decreases* in the Municipality's net assets are one indicator of whether its *financial health* is improving or deteriorating. You will need to consider other non-financial factors, however, such as changes in the Municipality's property tax base and the condition of the roads, to assess the *overall health* of the Municipality of Ponce.

In the Statement of Net Assets and the Statement of Activities, we divide the Municipality into two kinds of activities:

- **Governmental activities** - Most of the Municipality's basic services are reported here, including the municipal police, public works, garbage disposal, public energy and health services, and general administration. Property taxes, municipal license tax, state and federal grants finance most of these activities.
- **Component units** - The Municipality includes two separate legal entities in its report, the Port of Ponce (POP) and the Corporación para el Desarrollo Económico de Proyectos Comerciales y de Vivienda de Ponce, C.D. (CODEPCOVI). Although legally separate, these "component units" are important because the Municipality is financially accountable for them.

Reporting the Municipality's Most Significant Funds

Fund Financial Statements

Our analysis of the Municipality's major funds begins on page 16. The Fund financial statements begin on page 26 and provide detailed information about the most significant funds, not the Municipality as a whole. Some funds are required to be established by bond covenants. The Municipality's basic services are reported in the governmental funds, that uses an accounting approach which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called *modified accrual* accounting, which measures cash and all other *financial* assets that can readily

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

be converted to cash. The governmental fund statements provide a detailed *short-term view* of the Municipality's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. We describe the relationship (or differences) between governmental *activities* (reported in the Statement of Net Assets and the Statement of Activities) and governmental *funds* in a reconciliation on pages 28 and 31 of this report.

THE MUNICIPALITY AS A WHOLE

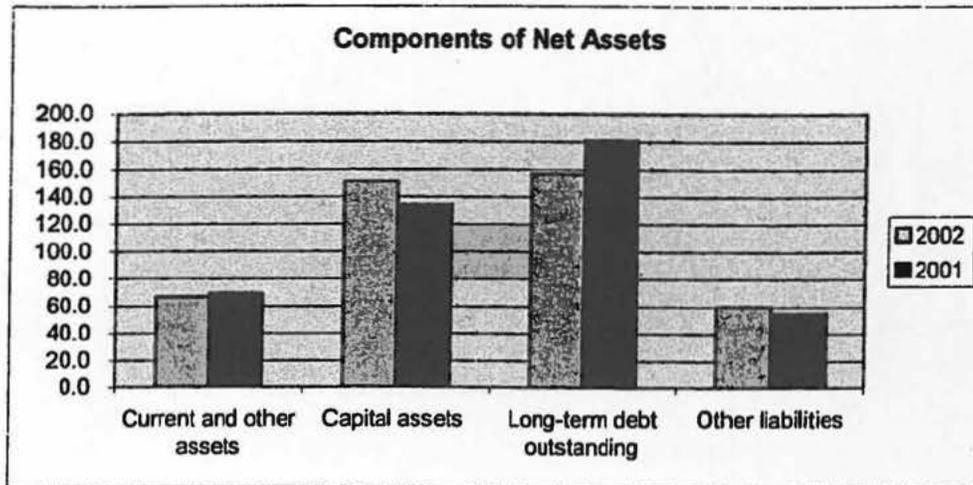
The Municipality's *combined* net assets increases from a year ago, from (\$32.2) million to \$.7 million. Our analysis below focuses on the net assets (Table 1) and changes in net assets (Table 3) of the Municipality's governmental and component unit's activities.

Table 1

**NET ASSETS
(in Millions)**

	<u>Governmental Activities</u>	
	<u>2002</u>	<u>2001</u>
Current and other assets	\$ 66.80	\$ 69.50
Capital assets	<u>151.10</u>	<u>134.20</u>
Total assets	<u>217.90</u>	<u>203.70</u>
Long-term debt outstanding	(156.90)	(181.00)
Other liabilities	<u>(60.30)</u>	<u>(54.90)</u>
Total liabilities	<u>(217.20)</u>	<u>(235.90)</u>
Net assets:		
Invested in capital assets, Net of related debt	79.40	34.30
Restricted for:		
Debt services	8.70	6.90
Capital project	31.00	38.40
Federal programs	0.10	0.16
Unrestricted	<u>(118.50)</u>	<u>(111.96)</u>
Net Assets	<u>\$ 0.70</u>	<u>\$ (32.20)</u>

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**



Net assets of the Municipality's governmental activities increased by 32.9 million ((32.2) million compared to \$.7 million). *Unrestricted* net assets, the part of net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements, changed from approximately \$(111.96) million at June 30, 2001 to a \$(118.50) million at June 30, 2002.

Governmental Activities

Revenues for the Municipality's governmental activities increased by 19% (\$21.5 millions), while total expenses increased by 17% (18.5 millions). The Municipality of Ponce took the following major actions this year to improve the financial position:

- The Mayor of the Municipality of Ponce made various committees to supervise the operations of all department of the Municipality. The component of those committee were meeting at lease one time per week. In those meetings the Mayor received different reports like a cash-flow, budget vs. actual, aging of account payable and a management report with an explanations of the movement of each account and the status of the account payable and expenses. The financial decisions of the Mayor were supported by those reports.
- In the budget respect the administration of the Municipality received the estimated of expenses by each department, and the Budget Director and the Mayor performed the evaluation to those expenses and determine the needed of each one, looking for the reduction of those unnecessary expenses without affecting the daily operations.

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

The increases in the general government expenditures during the fiscal year ended June 30, 2002 was substantially related to the following:

Table 2

**Governmental Activities
(in Millions)**

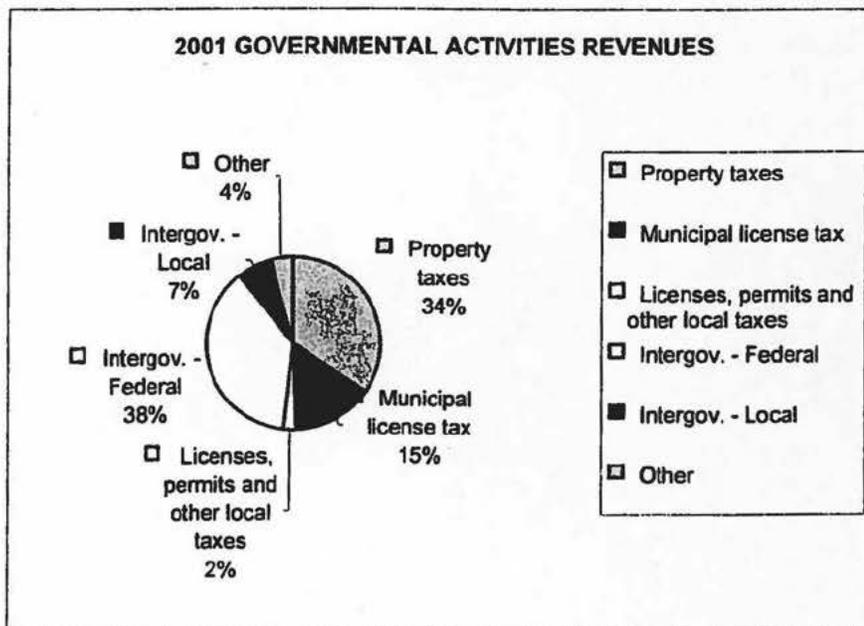
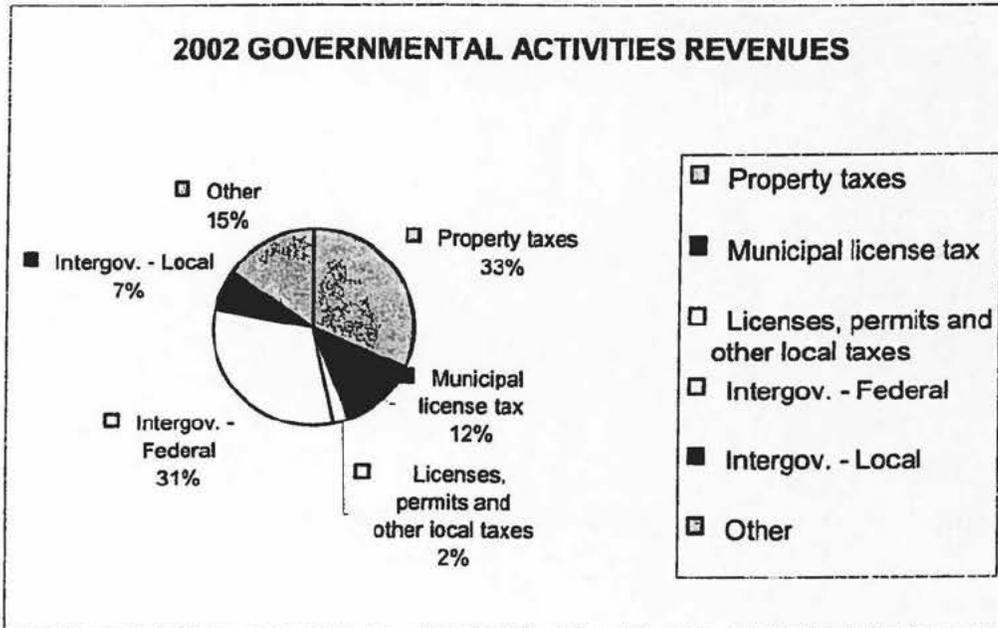
	Total cost of services	
	2002	2001
General Government	\$ 32.60	\$ 23.80
Health and welfare	26.50	33.00
Public Works	17.40	14.30
Education	10.60	9.60
Public Safety	9.10	7.60
 Totals	 \$ 96.20	 \$ 88.30

- Technical assistance required from Central Government Administration related to soil studies as part of the Las Americas Port,
- Technical assistance related to the compulsory implementation of the Governmental Accounting Standard Number 34, GASB 34,
- Legal assistance required in various cases against Central Government Agencies.
- During the year ended June 30, 2002 the Legislature of Puerto Rico enacted a Law ordering the increase in all governmental employees Christmas Bonus. The impact in the general fund was approximately \$300,000.

The major governmental revenue sources are property taxes, municipal license taxes, license and permits and grant and contributions not restricted, which in total represent \$112,932,189 (83%) and \$110,209,796 (94%) of all revenues in 2002 and 2001, respectively. Changes within these four sources of revenues were \$2.7 million.

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

The cost of all governmental activities this year was \$129.8 million compared to \$108.6 million last year. Table 2 presents the cost of each of the Municipality of Ponce's largest programs.



**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

THE MUNICIPALITY'S FUND

As the Municipality completed the year, its governmental funds (as presented in the balance sheet on pages 26 - 27) reported a combined fund balance of \$23.5 million, which is lower than last year total of \$29.4 million.

In addition, these other changes in fund balances should be noted:

- The Municipality experienced an increase in the collection of Licenses and Permits due to the developments of construction project which began during the year. The taxes paid to the Municipality related to those constructions permits increases as result of the developments of the city organization plan,
- During this year the Municipality received payments from Central Government and Governmental Agencies as reimbursement and partial settled of various cases. Those amounts are classified this year as part of other revenues because all reimbursements amounts are related with expenses incurred by the Municipality in prior years. The detail of these amounts are as follow:

*\$2.875 millions received as reimbursement from Puerto Rico Power Authority due to prior years excessive billing on public lighting,

* \$1.931 millions as reimbursement from Municipal Revenue Collection Center related to an incorrect retention during the last 3 years,

*\$9 millions received from Central Government as part of the amount due to the municipality from Ponce en Marcha case.

General Fund Budgetary Highlights

Over the course of the year, the Municipal Assembly revised the Municipality of Ponce budget several times. These budget amendments fall into various categories. The first category includes amendments and supplemental appropriations that were approved shortly after the beginning of the year and reflect the actual beginning balances (versus the amounts we estimated in May 2001). The second category includes changes that the Municipal Assembly made to take into consideration the amount received from CRIM related to a reimbursement of \$916,922, claim by the Municipality to CRIM for an incorrect retention of administrative expenses. See note 15 on the financial statements for further explanation.

Even with these adjustments, the actual changes to appropriations (expenditures) were \$99,004 thousand above the final budget amounts. The most significant negative variance (\$673,487) occurred in the intergovernmental revenues (state contribution account), because the municipality include as part of the state contribution the amount expected to be collected as indirect cost. These amounts was misclassify because the

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

indirect cost should be classify as an expenses reduction. However, this amount related to indirect cost is properly recorded in the financial statement as an expense reduction.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

As of June 30, 2002, the Municipality of Ponce had \$185 million invested in a broad range of capital assets, including buildings, parks, roads, bridges, and equipment. (See Table 4). This amount represents a net increase (including additions and deductions) of just over \$9 million, or 5 percent, over last year.

**Table 4
Capital Assets at Year End
(Net of Depreciation, in Thousands)**

	Governmental Activities	
	<u>2002</u>	<u>2001</u>
Land	\$ 28.70	\$ 28.60
Buildings and improvements	77.60	77.50
Construction in progress	22.80	7.60
Equipment	13.20	12.50
Infrastructure	<u>43.30</u>	<u>42.50</u>
 Totals	 <u>\$ 185.60</u>	 <u>\$ 168.70</u>

The City's fiscal-year 2003 capital budget call for it to spend another \$40 million for capital projects, principally for the port of Ponce. The Municipality has plans to issue additional debt to finance this project. More detailed information about the Municipality's capital assets is presented in Note 10 to the financial statements.

Debt

At year-end, the Municipality had \$ 95.6 million in bonds and notes outstanding versus \$ 102.9 million last year, a decrease of 7.6 percent, as shown in Table 5.

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

**Table 5
Outstanding Debt at Year End
(in Thousands)**

	Governmental Activities	
	2002	2001
Bonds payable	\$ 75.30	\$ 80.70
Government Development Bank	20.30	22.20
Loan Guarantee Assistance Notes	16.80	19.20
Advances from CRIM	50.50	50.50
Other obligations	10.50	23.20
Totals	\$ 173.40	\$ 195.80

New bonds in the amount of \$2 million were issued to finance improvements at the Municipal Port of Ponce. The Municipality is required to limit the amount of general obligation debt to 10% of the total assessment of property located within the Municipality, for bonds to be repaid with the proceeds of property taxes restricted for debt services. Other obligations include accrued vacation and sick leave, claims and judgments, and landfill obligation. More detailed information about the Municipality's long-term liabilities is presented in Note 14 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's elected and appointed officials considered many factors when setting the fiscal-year 2003 budget. Unemployment in the Municipality now stands at 12.3 percent.

Amounts available for appropriations in the General Fund for the fiscal year 2003 are \$80.8 million, an increase of 4 percent over the final 2002 budget of \$77.7 million. In overall the consolidated budget for the fiscal year 2003 is \$129 million, an increase of 4.3 percent over the 2002 budget of \$123.7 million. Construction excise taxes are expected to increase to \$8.2 million in 2003 from \$2.2 million in 2003, due to all scheduled construction of the Ponce en Marcha project, the Municipality's own public investment and the private sector investment. The Municipality will use these increases in revenues to finance programs we currently offer and the effect inflation will have on this programs.

Budgeted expenditures are expected to rise accordingly to the increase in budgeted revenues. Municipal police department budgeted expenditures are expected to be \$8.8 million, over \$3.6 million from fiscal year 2002. This new budgeted amount is necessary to cover the increase to a total of 420 municipal policemen.

**MUNICIPALITY OF PONCE, PUERTO RICO
MANAGEMENT' S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2002**

If these estimates are realized, the Municipality's budgetary General Fund balance is expected to increase modestly by the close of 2003.

CONTACTING THE MUNICIPALITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and creditors with a general overview of the Municipality's finances and to show the accountability for the money it receives. If you have questions about this report or need additional financial information, contact us at Municipality of Ponce, PO Box 331709, Ponce, Puerto Rico 00733-1709.

**GOBIERNO MUNICIPAL AUTÓNOMO
DE PONCE
OFICINA DE AUDITORIA INTERNA
APARTADO 1709
PONCE, P.R. 00733-1708**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
STATEMENT OF NET ASSETS
JUNE 30, 2002**

<u>Assets</u>	<u>Primary Government Governmental Activities</u>	<u>Component Units</u>	
		<u>CODEPCOVI</u>	<u>Port of Ponce</u>
Cash and cash equivalents (Note 2)	\$ 12,598,239	\$ 191,988	\$ 3,142,029
Cash with fiscal agent (Note 2)	46,962,812		
Loans and accounts receivable		99,093	187,705
Due from other agencies (Note 9)	3,789,937		
Other assets		21,370	113,300
Restricted assets:			
Cash held in escrow account for landfill closure and postclosure care costs (Note 19)	3,403,668		
Real estate projects under construction		12,354,948	
Capital assets, net (Note 10)	<u>151,162,320</u>	<u>12,667,399</u>	<u>3,443,034</u>
Total assets	<u>\$217,916,976</u>	<u>\$12,667,399</u>	<u>\$ 3,443,034</u>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
STATEMENT OF NET ASSETS
JUNE 30, 2002**

<u>Liabilities and Net Assets</u>	<u>Primary Government Governmental Activities</u>	<u>Component Units</u>	
		<u>CODEPCOVI</u>	<u>Port of Ponce</u>
Liabilities			
Accounts payable and accrued liabilities	\$ 14,203,327	\$ 4,516,741	\$ 505,793
Due to other agencies (Note 11)	1,217,033		
Deferred revenues:			
Municipal license tax (Note 13)	14,428,134		
Federal government (Note 13)	5,917,460		
Accrued interest	8,109,487		
Noncurrent liabilities (Note 14):			
Due within one year	16,444,103	6,501,427	
Due in more than one year	156,901,193	7,928	
Total liabilities	<u>217,220,737</u>	<u>11,026,096</u>	<u>505,793</u>
Net Assets			
Investment in capital assets, net of related debt	79,436,909		
Restricted for:			
Federal programs	123,073		
Debt service	8,663,131		
Capital projects	31,000,766		
Unrestricted	<u>(118,527,640)</u>	<u>1,641,303</u>	<u>2,924,689</u>
Total net assets	<u>\$ 696,239</u>	<u>\$ 1,641,303</u>	<u>\$ 2,924,689</u>

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

<u>Functions/Programs</u>	<u>Program Revenues</u>				<u>Net (Expense) Revenue and Changes in Net Assets</u>		
	<u>Expenses</u>	<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>	<u>Primary</u>	<u>Component Units</u>	
					<u>Governmental Activities</u>	<u>CODEPCOVI</u>	<u>Port of Ponce</u>
Primary Government:							
General government	\$ 32,626,262	\$ -	\$ -	\$ -	\$ (32,626,262)	\$ -	\$ -
Public safety	9,114,264				(9,114,264)		
Public works	17,469,797			1,897,998	(15,571,799)		
Culture and recreation	7,763,733	563,349			(7,200,384)		
Health and welfare	26,523,136		15,190,491		(11,332,645)		
Urban development	16,767,127		16,608,703		(158,424)		
Legal services	852,146				(852,146)		
Education	10,654,550		10,651,201		(3,349)		
Interest on long-term debt	8,109,487				(8,109,487)		
Total primary government	\$ 129,880,502	\$ 563,349	\$ 42,450,395	\$ 1,897,998	(84,968,760)	-	-
Component Units:							
CODEPCOVI	3,750,429	2,987,983	447,500			(314,946)	
Port of Ponce	2,110,533	2,125,953					15,420
Total component units	\$ 5,860,962	\$ 5,113,936	\$ 447,500	\$ -	-	(314,946)	15,420
General revenues:							
Property taxes					43,025,904		
Municipal license tax					16,927,289		
Royalties and others					1,816,746		
Licences, permits and other local taxes					3,284,751		
Grants and contributions not restricted to specific programs					7,243,850		
Interest and investment earnings					2,189,785	5,894	
Miscellaneous					16,193,370	15,250	136,454
Total general revenues					90,681,695	21,144	136,454
Change in net assets					5,712,935	(293,802)	151,874
Net assets at beginning of year					(5,016,696)	1,935,105	2,772,815
Net assets at end of year					\$ 696,239	\$ 1,641,303	\$ 2,924,689

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
BALANCE SHEET-GOVERNMENTAL FUNDS
JUNE 30, 2002**

<u>Assets</u>	<u>General</u>	<u>HUD Programs</u>	<u>Workforce Investment Act Program</u>	<u>Head Start Program</u>	<u>Debt Service</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Cash and cash equivalents (Note 2)	\$ 8,836,880	\$ 1,657,666	\$ 747,938	\$ 696,020	\$ -	\$ 659,735	\$ 12,598,239
Cash with fiscal agent (Note 2)	31,000,766				15,962,046		46,962,812
Due from other agencies (Note 9)		391,497	1,364,390	853,372	164,955	1,015,723	3,789,937
Advances to other funds (Note 8)	342,577	2,619,579		1,315			2,963,471
Restricted assets:							
Cash held in escrow account for landfill closure and postclosure care costs (Note 19)	3,403,668						3,403,668
Total assets	\$ 43,583,891	\$ 4,668,742	\$ 2,112,328	\$ 1,550,707	\$ 16,127,001	\$ 1,675,458	\$ 69,718,127

The accompanying notes are an integral part of these financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
BALANCE SHEET-GOVERNMENTAL FUNDS
JUNE 30, 2002**

<u>Liabilities and Fund Balance</u>	<u>General</u>	<u>HUD Programs</u>	<u>Workforce Investment Act Program</u>	<u>Head Start Program</u>	<u>Debt Service</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Liabilities							
Account payable and accrued liabilities	\$ 10,579,238	\$ 876,361	\$ 1,339,515	\$ 755,423	\$ -	\$ 652,790	\$ 14,203,327
Due to other agencies (Note 11)	1,217,033						1,217,033
Advances from other funds (Note 8)	2,620,858	23,261				319,352	2,963,471
General obligations:							
Bonds					5,360,000		5,360,000
Interest					2,103,870		2,103,870
Deferred revenues:							
Municipal license tax (Note 13)	14,428,134						14,428,134
Federal government (Note 13)		3,662,220	772,813	795,284		687,143	5,917,460
Total liabilities	<u>28,845,263</u>	<u>4,561,842</u>	<u>2,112,328</u>	<u>1,550,707</u>	<u>7,463,870</u>	<u>1,659,285</u>	<u>46,193,295</u>
Fund Balances							
Reserved for:							
Encumbrances	99,004						99,004
Federal programs		106,900				16,173	123,073
Debt service					8,663,131		8,663,131
Advances	342,577						342,577
Landfill closure and postclosure care costs	3,400,000						3,400,000
Capital projects	31,000,766						31,000,766
Deficiency	(20,103,719)						(20,103,719)
Total fund balance	<u>14,738,628</u>	<u>106,900</u>	<u>-</u>	<u>-</u>	<u>8,663,131</u>	<u>16,173</u>	<u>23,524,832</u>
Total liabilities and fund balance	<u>\$ 43,583,891</u>	<u>\$ 4,668,742</u>	<u>\$ 2,112,328</u>	<u>\$ 1,550,707</u>	<u>\$ 16,127,001</u>	<u>\$ 1,675,458</u>	<u>\$ 69,718,127</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO STATEMENT OF NET ASSETS
JUNE 30, 2002**

Total fund balances - governmental funds	\$23,524,832
Amounts reported for governmental activities in the statement of net assets are different because:	
• Capital assets used in governmental activities are not current financial resources and therefore are not reported in the governmental funds balance sheet	151,162,320
• Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds. (Note 4)	(<u>173,990,913</u>)
Net assets of governmental activities	\$ <u>696,239</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES-GOVERNMENTAL FUNDS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

	General	HUD Programs	Workforce Investment Act Program	Head Start Program	Debt Service	Other Governmental Funds	Total Governmental Funds
REVENUES							
Property taxes (Note 6)	\$31,047,148	\$ -	\$ -	\$ -	\$ 11,978,756	\$ -	\$ 43,025,904
Municipal license taxes (Note 7)	16,927,289						16,927,289
Royalties and other	1,816,746						1,816,746
Licenses and permits	3,284,751						3,284,751
Charges for service and rents	563,349						563,349
Intergovernmental revenues (Note 12):							
Federal grants and contributions		16,608,703	10,651,201	13,007,334		2,183,157	42,450,395
State contributions	9,141,848						9,141,848
Interest, fines, and penalties	2,040,484				149,301		2,189,785
Other revenues	16,193,370						16,193,370
Total revenues	<u>81,014,985</u>	<u>16,608,703</u>	<u>10,651,201</u>	<u>13,007,334</u>	<u>12,128,057</u>	<u>2,183,157</u>	<u>135,593,437</u>
EXPENDITURES							
General government	29,712,061						29,712,061
Public safety	8,979,368						8,979,368
Public works	16,490,889						16,490,889
Culture and recreation	7,510,837						7,510,837
Health and welfare	10,779,890			13,007,334		2,183,157	25,970,381
Urban development	-	16,648,032					16,648,032
Legal services	852,146						852,146
Education	-		10,651,201				10,651,201
Capital outlays	11,478,985						11,478,985
Debt service:							
Principal	3,910,558				5,360,000		9,270,558
Interest and other	1,082,302				4,807,463		5,889,765
Total expenditures	<u>90,797,036</u>	<u>16,648,032</u>	<u>10,651,201</u>	<u>13,007,334</u>	<u>10,167,463</u>	<u>2,183,157</u>	<u>143,454,223</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(9,782,051)</u>	<u>(39,329)</u>	<u>-</u>	<u>-</u>	<u>1,960,594</u>	<u>-</u>	<u>(7,860,786)</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES-GOVERNMENTAL FUNDS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

	<u>General</u>	<u>HUD Programs</u>	<u>Workforce Investment Act Program</u>	<u>Head Start Program</u>	<u>Debt Service</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
OTHER FINANCING SOURCES (USES)							
Loan proceeds	\$ 2,000,000	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 2,000,000
Transfers in	215,723						215,723
Transfers out					(215,723)		(215,723)
Total other financing sources (uses)	<u>2,215,723</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(215,723)</u>	<u>-</u>	<u>2,000,000</u>
Net change in fund balance	(7,566,328)	(39,329)	-	-	1,744,871	-	(5,860,786)
FUND BALANCE AT BEGINNING OF YEAR	<u>22,304,956</u>	<u>146,229</u>			<u>6,918,260</u>	<u>16,173</u>	<u>29,385,618</u>
FUND BALANCE AT END OF YEAR	<u>\$14,738,628</u>	<u>\$ 106,900</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,663,131</u>	<u>\$ 16,173</u>	<u>\$ 23,524,832</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

Net change in fund balances - total governmental funds (\$5,860,786)

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

- Governmental funds report capital outlays as expenditures. However, in the statement of activities and changes in net assets, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount of capital assets recorded in the current period. 11,478,985
- Governmental funds report principal payments on long-term obligations as expenditures, whereas the principal payments reduces the long-term obligations in the statement of activities. 9,270,558
- Governmental funds report issuance of long-term debt as other financial sources because provides current financial resources. (2,000,000)
- Depreciation expense on capital assets is reported in the statement of activities, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditure in governmental funds. (2,956,100)
- Change in accrued interest expense which does not require the use of current financial resources. (2,219,722)
- Some expenses reported in the statement of activities do not require the use of current financial resources; therefore, are not reported as expenditures in governmental funds. (2,000,000)

Changes in net assets of governmental activities \$ 5,712,935

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
STATEMENT OF REVENUES AND EXPENDITURES - GENERAL AND DEBT SERVICE FUNDS - BUDGET AND ACTUAL
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

	General Fund				Debt Service Fund			
	Budgeted Amounts		Actual	Variance with Final Budget- Positive (Negative)	Budgeted Amounts		Actual	Variance with Final Budget- Positive (Negative)
	Original	Final			Original	Final		
REVENUES								
Property taxes	\$ 31,443,237	\$ 31,443,237	\$ 31,047,148	\$ (396,089)	\$ 8,905,063	\$ 8,905,063	\$ 11,978,756	\$ 3,073,693
Municipal license taxes	17,175,000	17,175,000	16,927,289	(247,711)				
Royalties and other	1,704,000	1,704,000	1,816,746	112,746				
Licenses and permits	2,315,000	2,315,000	3,284,751	969,751				
Charges for service and rents	464,350	464,350	563,349	98,999				
Intergovernmental revenues:								
State contributions	7,659,911	7,659,911	6,986,424	(673,487)				
Interest, fines and penalties	2,020,000	2,020,000	2,040,484	20,484			149,301	149,301
Other revenues	14,912,865	15,829,771	16,193,370	363,599				
Total revenues	<u>77,694,363</u>	<u>78,611,269</u>	<u>78,859,561</u>	<u>248,292</u>	<u>8,905,063</u>	<u>8,905,063</u>	<u>12,128,057</u>	<u>3,222,994</u>
EXPENDITURES								
General government	32,951,698	28,982,944	29,224,760	(241,816)				
Public safety	6,599,398	8,979,368	8,972,120	7,248				
Public works	14,619,912	16,530,489	16,445,449	85,040				
Culture and recreation	6,836,732	7,493,572	7,518,977	(25,405)				
Health and welfare	10,411,467	10,779,890	10,779,281	609				
Legal services	812,981	852,146	769,143	83,003				
Debt service:				-				
Principal	5,462,175	3,910,558	3,910,558	-	5,013,023	5,013,023	5,360,000	346,977
Interest		1,082,302	1,082,302	-	3,892,040	3,892,040	4,807,463	915,423
Total expenditures	<u>77,694,363</u>	<u>78,611,269</u>	<u>78,702,590</u>	<u>(91,321)</u>	<u>8,905,063</u>	<u>8,905,063</u>	<u>10,167,463</u>	<u>1,262,400</u>
Excess of revenues over expenditures	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 156,971</u>	<u>\$ 156,971</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,960,594</u>	<u>\$ 1,960,594</u>

The accompanying notes are an integral part of these basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

1. ORGANIZATION

The Municipality of Ponce, Puerto Rico (Municipality) was founded in 1692. The Municipality is a political legal entity with full legislative and administrative faculties in every affair of municipal character, with perpetual succession existence and legal identity, separate and independent from the central government of the Commonwealth of Puerto Rico. The Municipality provides a full range of services including: public safety, public works, culture, recreation, health and welfare, education and other miscellaneous services.

The Municipal Government comprises the executive and legislative branches. The executive power is exercised by the Mayor and the legislative by the Municipal Assembly, which has 16 members. The members of these branches are elected every four years in the Puerto Rico general elections.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the Municipality have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental entities. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

For fiscal year ended June 30, 2002, the Municipality implemented GASB Statement No. 33 (GASB 33), Accounting and Financial Reporting for Nonexchange Transactions; GASB Statement No. 34 (GASB 34), Basic Financial Statements - Management's Discussion and Analysis - for State and Local Governments; GASB Statement No. 36 (GASB 36), Recipient Reporting for Certain Shared Non exchange Revenues (and amendment of GASB 33); GASB Statement No. 37 (GASB 37), Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments: Omnibus; GASB Statement No. 38 (GASB 38), Certain Financial Statements Disclosures; and GASB Interpretation No. 6, Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements.

GASB 34, as amended by GASB 37, establishes new requirements and a new reporting model for the financial statements of state and local governments. GASB 34 was developed to make the financial statements easier to understand and more

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

useful to the people who use governmental financial information to make decisions and includes:

- **Management's Discussion and Analysis - GASB 34** requires the financial statements be accompanied by a narrative introduction and analytical overview of the government's financial activities in the form of management's discussion and analysis (MD&A).
- **Government - Wide Financial Statements -** The new reporting model includes financial statements prepared using full accrual of accounting for all of the government's activities. This approach includes not just current assets and liabilities, but also capital assets and long-term liabilities (such as buildings and infrastructure, including bridges and roads, and general obligation debt).
- **Statement of Net Assets -** The statement of net assets is designed to display the financial position of the Municipality, including capital assets and infrastructure. The net assets of the Municipality will be broken down into three categories; invested in capital assets, net of related debt; restricted; and unrestricted.
- **Statement of Program Activities -** The new government - wide statement of activities report expenses and revenues in a format that focuses on the cost of each of the government's functions. The expense of individual functions is compared to the revenues generated directly by the function.
- **Budgetary comparison schedules -** Demonstrating compliance with the adopted budget is an important component of a government's accountability to the public. Under the new reporting model, the Municipality will continue to provide budgetary comparison information in their financial statements. An important change, however, is a requirement to add the government's original budget to the current comparison of final budget and actual results.

GASB 33, as amended by GASB 36, establishes standards for recording non-exchange transactions on the modified accrual and accrual basis of accounting.

GASB 38 establishes and modifies disclosure requirements related to the summary of significant accounting policies, actions taken to address violations of significant finance - related legal and contractual provisions, debt and lease obligations, short-term debt, disaggregation of receivable and payable balances, and interfund balances and transfers with GASB 34 is implemented.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

The following is a summary of the more significant policies:

a. Reporting Entity

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, "The Financial Reporting Entity", of the GASB. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exist 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 units' balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component units' financial data in columns separate from the Municipality's balances and transactions.

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

Port of Ponce (POP) was formed as a result of an ordinance, dated November 20, 1911, and enacted by the Executive Council of Puerto Rico, which granted the Municipality authority to construct, maintain and operate a pier, on the shore of the Ponce Harbor. The operations of the port facilities are financed principally through charges to users.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

Corporación para el Desarrollo Económico de Proyectos Comerciales y de Vivienda de Ponce, C.D. (CODEPCOVI) was incorporated on September 23, 1985, as a public nonprofit corporation to promote the economic development of the City of Ponce, originally under the name of Ponce Economic Development Corporation. CODEPCOVI'S principal activity consists of granting loans to small businesses. CODEPCOVI'S activities are principally financed through contributions from the Municipality using federal assistance and interest charges to borrowers.

Separate financial statements of the individual component units can be obtained from their respective administrative offices.

Administrative offices:

Port of Ponce
Carretera 10 final
Playa de Ponce
Ponce, Puerto Rico 00731

Corporación para el Desarrollo Económico de Proyectos Comerciales y de Vivienda de Ponce, C. D.
Condominio Ponciana 3-D
Marina 16
Ponce, Puerto Rico 00731

b. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all the activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities which normally are supported mainly by taxes and intergovernmental revenues are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) 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.

The fund financial statements segregate transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

c. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The government-wide financial statements are reported using the *economic resources measurement focus*. 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.

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 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, licenses, 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. Only the portion of special

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The Municipality reports the following major governmental funds:

1) General Fund

This is the operating fund of the Municipality and accounts for all financial resources, except those required to be accounted for in another fund.

2) HUD Programs Fund

This fund accounts for revenue sources for the development of viable urban communities, decent housing, suitable living environment, rental assistance to help very low-income families afford decent, safe and sanitary housing by encouraging property owners to rehabilitate substandard housing and lease the units with rental subsidies to low income families.

3) Workforce Investment Act Fund

This fund accounts for revenue sources to help people access the tools they need to manage their careers through information and high quality services and to help U. S. companies find skilled workers.

4) Head Start Program Fund

This fund accounts for revenue sources to provide comprehensive health, educational, nutritional, social and other services to economically disadvantaged pre-school children so that the children will attain overall social competence.

5) Debt Service Fund

This fund accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, 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 government has elected not to follow subsequent private-sector guidance.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements.

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. 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, than unrestricted resources as they are needed.

d. Cash, Cash Equivalents, and Cash with Fiscal Agent

The Municipality's Finance Director is responsible for investing available resources. The Municipality is restricted by law to invest only in savings accounts and certificates of deposit with banks qualified as a depository of public funds by the Puerto Rico Treasury Department (PRTD) or in instruments of the Government Development Bank for Puerto Rico (GDB). The Municipality's policy is to invest any excess cash in interest bearing deposits with institutions qualified by the PRTD. Earnings from these funds are recorded in the corresponding fund.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

Cash and cash equivalents of the component units are maintained in their own names in bank accounts separate from those of the primary government.

The Municipality consider all investments with an original maturity of three months or less to be cash equivalents.

e. Receivables

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 special revenue fund represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs.

Loans and accounts receivable of the discretely presented component units are mainly composed of low-income housing mortgages, commercial loans, and charges for services, net of estimated allowances for uncollectible amounts.

f. Interfund 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.

g. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure (which is normally immovable and of value only to the Municipality, such as roads, bridges, streets sidewalks, and drainage system), are reported in the applicable governmental or component units columns in the government-wide financial statements.

Capital assets purchased or acquired are carried at historical cost or estimated historical cost. Contributed assets are recorded at fair market value as of the date donated. Additions, improvements and other capital outlays that significantly

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred.

Depreciation in capital assets is calculated on the straight-line basis over the following estimated useful lives:

	<u>Useful Life</u>
Buildings and building improvements	20-50 years
Land improvements	20-30 years
Machinery and equipment	5-20 years
Infrastructure	20-50 years

h. Real Estate Projects under Construction

Real estate projects under construction represent the cost of acquisition of real estate and other construction costs incurred by CODEPCOVI for the purpose of developing low-income housing projects for sale to qualifying applicants.

i. Reservation of Fund Balance

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

1) Encumbrances

Represents 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.

2) Federal Programs

Represents the reservations of amounts available for specific use under federal grant programs.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

3) Advances

Represents the reservations of amounts advanced among the funds of the primary government which are not considered to be current available financial resources.

4) Landfill Closure and Postclosure Care Costs

Represents the reservation of the amount required to be held and deposited in an escrow account to cover the closure and postclosure care costs of the municipal solid waste landfill facilities. At June 30, 2002, the amount reserved for landfill and postclosure care costs was \$3,400,000.

5) Debt Service

Represents net assets available to finance future debt service payments.

6) Capital Project Funds

Represents the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. The committed amounts generally will become liabilities in future periods as the projects are completed.

j. **Risk Financing**

The Municipality carries 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 (the "CRIM") for the year ended June 30, 2002 amounted to approximately \$1.9 million. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$2.1 million for workers compensation insurance covering all municipal employees. Settled claims have not exceeded commercial coverage in any of the past three fiscal years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

k. Compensated Absences

Employees accumulate vacation leave at a rate of 2.5 days per month up to maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum 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.

l. Use of Estimates

The preparation of 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, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

m. Reclassifications to Component Units Amounts

Certain reclassifications have been made to the amounts presented in the separately issued component units financial statements to conform to the presentation used in the Municipality's basic financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

n. Future Adoption of Accounting Pronouncements

The Governmental Accounting Standards Board has issued the following statement that the Municipality or its component units have not yet adopted:

<u>Statement Number</u>		<u>Adoption Required in Fiscal Year</u>
39	Determining Whether Certain Organizations are Component Units, an Amendment of GASB Statements No. 14.	2003-04

The impact of this statement on the Municipality's financial statements has not yet been determined.

3. 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 Assembly prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Assembly. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Assembly.

The Municipality prepares its annual budget including the operations of the general and the debt service funds.

Revenues and Expenditures - Budget and Actual (Budgetary Basis), accordingly, includes only the operations of the general and the debt service funds. The amounts budgeted under the Special Revenue Fund were excluded since they are received and expended over a period of time which generally exceeds the current year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

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 Assembly has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The annual budget is presented in the Combined Statement of Revenues and Expenditures - Budget and Actual (Budgetary Basis) is the budget ordinance to June 30, 2002 representing the original budget.

b. Budget/GAAP Reconciliation

The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of entity and timing differences in the excess of revenues and other financing sources over expenditures and other financing uses for the year ended June 30, 2002 is presented below for the general, and debt service funds:

	<u>General</u>	<u>Debt Service</u>
Excess of revenues over expenditures - budgetary basis	\$ 156,971	\$1,960,594
Entity differences:		
Non-budgeted funds	(7,739,722)	
Non-budgeted transfers	215,723	(215,723)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

	<u>General</u>	<u>Debt Service</u>
Timing differences:		
Prior year encumbrances recorded as current year expenditures for GAAP basis	(\$ 298,304)	\$
Current year encumbrances recorded as expenditures for budgetary purposes	99,004	_____
Excess (deficiency) of revenues over (under) expenditures - GAAP basis	(\$7,566,328)	\$1,744,871

c. Legal Compliance

The legal level of budgetary control is at the individual department level for general fund expenditures, and principal and interest due for the debt service fund.

4. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

Explanation of certain differences between governmental fund balance sheet and the government-wide statement of net assets.

The governmental fund balance sheet includes a reconciliation between fund balance-governmental funds and net assets of governmental activities as reported in the government-wide statement of net assets. One element of that reconciliation explains that some liabilities, including bonds and notes payable, are not due and payable in the current period and therefore are not reported in the funds. The details of this \$171,953,767 difference are as follows:

Bonds and notes payable	\$107,007,322
Advances from CRIM	50,533,654
Accrued interest payable	6,005,617
Compensated absences	8,407,174
Net adjustment to reduce fund balance governmental funds to arrive at net assets of governmental activities	\$171,953,767

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

5. DEPOSITS AND INVESTMENTS

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 \$9.7 million in the general fund were fully collateralized at June 30, 2002. The deposits at GDB of approximately \$3.4 million that are restricted principally for capital projects, and the \$16.0 million in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

The excess is covered by collateral provided by banks and held by the Treasury Department of the Commonwealth of Puerto Rico pursuant to applicable laws and regulations.

6. PROPERTY TAXES

The Municipal Revenues Collection Center (CRIM) of the Commonwealth of Puerto Rico is responsible by law for the assessment, levy and collection of all real and personal property taxes. The tax on personal property is self assessed by the taxpayer. The assessment is made in a return which must be filed with the CRIM by May 15 of each year. The tax on real property is assessed by the CRIM. The assessment is made as of January 1 of each year and is based on estimated current values of the property as of year 1957. The tax on personal property must be paid in full together with the return on or before May 15. The tax on real property is due in two equal installments in July 1 and January 1, following the assessment date.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

The rates are 8.33% for real property and 6.33% for personal property. The composition is as follows:

	<u>Real</u>	<u>Personal</u>
Basic property	6.00%	4.00%
Additional special property - state	1.03%	1.03%
Additional special property - municipal	1.50%	1.50%
Discounts made by state to tax payer	< .20%>	< .20%>
	<u>8.33%</u>	<u>6.33%</u>

The Municipality's basic property tax rate represents the portion which is appropriated for general purposes and accounted for in the general fund.

The "Additional special property tax - municipal" is restricted for debt service and retained by GDB for such purposes and it is recorded as revenue in the Debt Service Fund when collected by the CRIM and reported to the Municipality.

The "Additional special property tax - state" is collected by the CRIM for the payment of principal and interest of general obligation bonds and certain other obligations issued by the state government.

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

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

Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collected 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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

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. Total advances from CRIM as of June 30, 2002, presented as noncurrent liabilities in the government-wide financial statements amounted to approximately \$50.5 million.

Currently, the Municipality has received the preliminary settlement from CRIM related to fiscal year 2001-02, but not the final settlement as the six months period after fiscal year end, provided by law to CRIM to issue this, has not yet expired. Management believes, based in part on the experience from prior years, that when received, the final settlement from CRIM will not show a significant difference from the preliminary settlement and that such difference, if any, will not have a material effect on the financial condition of the Municipality.

Based on the preliminary settlement already received, during the year ended June 30, 2002, the amount received in advances from CRIM exceeded the amount collected from taxpayers and charges by CRIM for the same period by approximately \$374,000. Such amount is presented as due to the agencies in the basic financial statements (refer to Note 11).

During the fiscal year ended June 30, 2002, transactions regarding property tax advances were as follows:

Due from the Municipal Revenues Collection	
Center June 30, 2001	\$ 1,334,017
Current year advances	(31,443,237)
Collection of property taxes	31,047,148
Payment received from CRIM	(916,922)
Adjustments	(<u>395,286</u>)
 Due to the Municipal Revenues Collection	
Center, June 30, 2002	(<u>\$ 374,280</u>)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

On January 26, 2000, Public Law 42, as amended, was enacted which authorized the CRIM to obtain a loan up to \$200 million, and for a term not exceeding 30 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 vs. actual collections through fiscal year 1999-2000. The amount that the municipalities will collect from the additional property taxes resulting from the increases in the subsidy from the central government 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.

7. MUNICIPAL LICENSE TAX

Municipal License Tax are recorded in the fiscal year in which payment is due and, accordingly, represent taxes which are due and uncollected at June 30, 2002. The annual Municipal License Tax is determined based on the gross income of all commerce and industrial organizations who have operations in the Municipality of Ponce, and are not totally or partially exempt under the Industrial Incentive Law of Puerto Rico.

An annual return of business volume should be filed on or before April 15 of each year and payable in two equal installments due on July 1 and January 1. A discount of 5% is allowed when full payment is made on or before April 15. The rates of municipal license in the Municipality of Ponce, are as follows:

Financing institution = 1.50% of gross revenues
Other organizations = .30% for annual sales up to \$500,000, and .50% over such volume

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

8. INTERFUND TRANSACTIONS

Interfund receivables and payables balances at June 30, 2002 consisted of the following:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
HUD	General Fund	\$2,619,579
General Fund	HUD	16,463
General Fund	Nonmajor Governmental Funds	326,114
Head Start	General Fund	<u>1,315</u>
		<u>\$2,963,471</u>

Interfund transfers between the general and debt service funds represent the interest income received from the CRIM.

9. DUE FROM OTHER AGENCIES

Represents grants and contributions due from local and federal agencies:

Department of Labor - WIA	\$1,364,390
HHS - Head Start	853,372
Federal Emergency Management Agency	740,096
HUD - HOME Program	327,711
HHS - Ryan White	222,061
Municipal Revenue Collection Center (CRIM)	164,976
HUD - Emergency Shelter	37,823
HUD - Initiative	25,963
Other	<u>53,545</u>
Total	<u>\$3,789,937</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

10. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2002 was as follows:

<u>Primary Government</u>	<u>Balance June 30, 2001</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2002</u>
Governmental Activities:				
Capital assets, not being depreciated:				
Land	\$ 24,327,718	\$ 112,000	\$ -	\$ 24,439,718
Construction in progress	7,611,429	15,210,693		22,822,122
Total capital assets, not being depreciated	<u>31,939,147</u>	<u>15,322,693</u>	<u>-</u>	<u>47,261,840</u>
Capital assets, being depreciated:				
Buildings and building improvements	77,546,609	53,105		77,599,714
Land improvements	4,339,196	18,065		4,357,261
Machinery and equipment	12,591,524	631,878		13,223,402
Infrastructure	42,520,663	799,796		43,320,459
Total capital assets, being depreciated	<u>136,997,992</u>	<u>1,502,844</u>	<u>-</u>	<u>138,500,836</u>
Less accumulated depreciation for:				
Buildings and building improvements	12,404,996	1,434,259		13,839,255
Land improvements	888,622	75,179		963,801
Machinery and equipment	7,867,822	667,145		8,534,967
Infrastructure	10,482,816	779,517		11,262,333
Total accumulated depreciation	<u>31,644,256</u>	<u>2,956,100</u>	<u>-</u>	<u>34,600,356</u>
Total capital assets, being depreciated, net	<u>105,353,736</u>	<u>(1,453,256)</u>	<u>-</u>	<u>103,900,480</u>
Governmental activities capital assets, net	<u>\$ 137,292,883</u>	<u>\$ 13,869,437</u>	<u>\$ -</u>	<u>\$ 151,162,320</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

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

General government	\$ 914,201
Public safety	134,896
Public works	978,908
Culture	252,896
Recreation	552,755
Health and welfare	119,095
Legal services	<u>3,349</u>
Total depreciation expense	<u>\$ 2,956,100</u>

11. DUE TO OTHER AGENCIES

Due to other agencies at June 30, 2002 are as follows:

Employee's Retirement System	\$ 634,029
Puerto Rico Electric Power Authority	208,724
Municipal Revenue Collection Center	<u>374,280</u>
Total	<u>\$1,217,033</u>

12. INTERGOVERNMENTAL REVENUES

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

Following is a detail of intergovernmental revenues:

Puerto Rico Electric Power Authority	\$6,224,911
Joint resolutions	1,897,998
Reimbursement from the Commonwealth of Puerto Rico of Christmas bonus expenditure	755,080
Citizen Participation for the Municipal Development Program - CRIM	<u>263,859</u>
Total	<u>\$9,141,848</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

13. DEFERRED REVENUES

a. Municipal License Tax

The deferred revenues of approximately \$14.4 million in the general fund related to municipal license tax collected in fiscal year 2001-02 that will be earned in fiscal year 2002-03.

b. Federal Government

The deferred revenues presented as federal government represents the portion of federal grants received for which qualifying expenditures have not been incurred. The amounts were determined taking into consideration the specific years of the grant. These were related to the following federal programs/grants:

Program/Grant Description

Head Start	\$ 795,284
Lower Income Housing Assistance and Section 8 Housing Voucher	1,478,060
Loan Guarantee Assistance	1,562,306
Workforce Investment Act	746,407
Welfare to Work	26,406
Community Development Block Grant	519,706
HUD Disaster Recovery Initiative-Hortense	70,000
Hurricane Georges	30,096
Housing Administration-St. Thomas	2,042
Home Devolution	184,507
Rental Rehabilitation	51,673
Local Law Enforcement	344,329
San Antón Project	<u>106,644</u>
Total	<u>\$5,917,460</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

14. LONG-TERM DEBT

Bonds and notes payable outstanding at June 30, 2002 consist of:

Bonds

1991 serial bonds due in annual installments of \$420,000 to \$1,415,000, through July 1, 2006; with interest ranging from 3.26% to 6.36%.	\$ 4,995,000
1992 serial bonds due in annual installments of \$150,000 to \$390,000, through July 1, 2007; with interest ranging from 4.16% to 6.41%.	1,710,000
1992 special obligations due in annual installments of \$440,000 to \$2,010,000, through July 1, 2012; with interest ranging from from 5% to 8%.	14,060,000
1997 general obligations due in annual installments of \$410,000 to \$1,220,000, through July 1, 2011; with interest ranging from 4.87% to 6.75%.	8,225,000
1997 general obligations due in annual installments of \$345,000 to \$695,000, through July 1, 2006; with interest ranging from 6% to 8%.	2,480,000
1999 general obligations due in annual installments of \$1,040,000 to \$1,990,000, through July 1, 2008; with interest ranging from 6% to 7.50%.	10,050,000
1999 general obligations due in annual installments of \$115,000 to \$320,000, through July 1, 2013; with interest ranging from 4.87% to 6.11%.	2,500,000
2000 general obligations due in annual installments of \$165,000 to \$230,000, through July 1, 2004; with interest ranging from 7.29% to 8%.	445,000

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

2001 general obligations bonds due in annual installments of \$435,000 to \$2,755,000, through July 1, 2025; with interest ranging from 6.13% to 8%.

\$30,860,000

Total outstanding bonds

\$75,325,000

Notes

\$32,000,000 note payable in semiannual payments of principal and interest of \$2,800,000 until July 2006 bearing interest at one half percent (½%) over the 90 days LIBOR rate.

\$18,297,322

\$2,000,000 note payable which will be repaid from a future bond issuance, bearing interest at 8% to be paid at maturity.

2,000,000

Total outstanding notes

20,297,322

Total bonds and notes payable

\$95,622,322

Loan Guarantee Assistance (LGA) Notes

These notes are payable in annual aggregate principal installments of \$2,500,000, plus interest rates which fluctuates from 8.04% to 8.19%. These notes are guaranteed by the federal government through the Loan Guarantee Assistance Program and will be repaid from future appropriations to the Municipality's Community Development Block Grant for Puerto Rico program.

Advances from CRIM

This amount represents the balances owed to CRIM at June 30, 2002 as described in Note 6, and that will be repaid through a financing to be obtained by the CRIM, as authorized by law and as explained in that note.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

Annual maturity requirements for the bonds and notes payable and loan guarantee assistance notes are as follows:

<u>Bonds Payable</u>	<u>Principal</u>	<u>Interest</u>
2003	\$ 5,785,000	\$ 5,610,318
2004	6,260,000	5,202,787
2005	6,530,000	4,759,378
2006	7,060,000	4,297,179
2007	5,340,000	3,795,439
2008-2011	17,195,000	11,657,797
2012-2016	8,570,000	9,151,322
2017-2021	8,735,000	6,143,200
2022-2025	9,850,000	2,046,000
	<u>\$ 75,325,000</u>	<u>\$ 52,663,420</u>
<u>Notes Payable</u>		
2003	\$ 6,159,103	\$ 1,381,886
2004	4,424,061	1,043,944
2005	4,706,520	684,460
2006	5,007,638	302,012
	<u>\$ 20,297,322</u>	<u>\$ 3,412,302</u>
<u>Loan Guarantee Assistance Notes</u>		
2003	\$ 2,500,000	\$ 1,117,283
2004	2,500,000	926,055
2005	2,505,000	734,135
2006	2,325,000	547,921
2007	1,210,000	413,832
2008-2011	2,940,000	1,026,464
2012-2016	2,765,000	446,989
	<u>\$ 16,745,000</u>	<u>\$ 5,212,679</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

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, 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. Total property assessed value at June 30, 2002 amounted to approximately \$825 million. Long-term debt, except for the bonds payable and the loan guarantee assistance notes, is paid with unrestricted funds.

Component Units

The notes payable by the discretely presented component units are owed by CODEPCOVI and are composed of the following:

CODEPCOVI

Construction loan bearing interest at 1.5% over the prime rate, collateralized by the Municipality and a mortgage note over real estate, due as housing units are sold.	\$6,497,740
---	-------------

Loan bearing interest at 7.9% payable in monthly installments of \$430 due in June 2005 secured by motor vehicles.	<u>11,615</u>
--	---------------

Total	<u>\$6,509,355</u>
-------	--------------------

Fixed maturities required to pay principal of CODEPCOVI motor vehicles loan were as follows:

2003	\$ 3,687
2004	3,927
2005	<u>4,001</u>
Total	<u>\$11,615</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

Long-term liability activity for the year ended June 30, 2002 was as follows:

Primary Government: Governmental Activities:	Beginning Balance	Additions	Reductions	Ending Balance	Due within One Year
Bonds payable	\$ 80,685,000	\$ -	\$ (5,360,000)	\$ 75,325,000	\$ 5,785,000
Notes payable	22,207,885	2,000,000	(3,910,563)	20,297,322	6,159,103
Loan guarantee assistance notes	19,245,000		(2,500,000)	16,745,000	2,500,000
Total bonds and payable	122,137,885	2,000,000	(11,770,563)	112,367,322	14,444,103
Advances from CRIM	50,533,654			50,533,654	
Claims and judgments	2,500,000		(2,500,000)	-	
Compensated absences	9,598,431	845,889	-	10,444,320	2,000,000
Total other liabilities, governmental activities	62,632,085	845,889	(2,500,000)	60,977,974	2,000,000
Total noncurrent liabilities, governmental activities	\$ 184,769,970	\$ 2,845,889	\$ (14,270,563)	\$ 173,345,296	\$ 16,444,103
Component Units:					
CODEPCOM:					
Notes payable	\$ 6,790,580	\$ -	\$ (281,225)	\$ 6,509,355	\$ 6,501,427

15. RETIREMENT PLAN

a. Plan Description

The Employee's Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) is the administrator of a cost-sharing multiple-employer retirement system established by the Commonwealth of Puerto Rico. The ERS was created under the ACT 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

ERS covers all regular employees of the Commonwealth of Puerto Rico and its instrumentalities and of certain municipalities and components units not covered by their own retirements systems.

Participation is mandatory except for members of the Legislature, Government Secretaries, Heads for Agencies and Public Instrumentalities, Assistants to the Governor, the Comptroller of Puerto Rico, Gubernatorial Board and Committee appointees and Experimental Service Station employees.

ERS provides retirement, death and disability benefits. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

Members who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained an age of at least fifty-eight (58) years and have completed at least fifty-eight (58) years and have completed at least ten (10) years of creditable service, are entitled to an annual benefit, payable monthly for life.

The amounts of the annuity shall be one and one-half percent of the average compensation multiplied by the number of years of creditable service up to twenty years, plus 2% of the average compensation multiplied by the number of years of creditable service in excess of twenty years. In no case the annuity will be less than \$200 per month.

Participants who have completed at least thirty (30) years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained fifty-five (55) years of age will receive 65% of the average compensation or if they have attained fifty-five (55) years of age will receive 75% of the average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of service.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created ERS, was enacted with the purpose of establishing a new pension program (System 2000). Employees participating 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 , 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. Benefits at retirement age will not be guaranteed by the Commonwealth of Puerto Rico. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% of the employee's salary upon to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

b. Contribution Requirements

Commonwealth legislation requires employees to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600. The Municipality's contributions are 9.275% of gross salary. Contributions' requirements are established by law. The actuarially determined contribution requirement and contributions actually made for the year ended June 30, 2002 was approximately \$3.2 million. The Municipality's payroll for employees covered by ERS was approximately \$34.6 million. The Municipality total payroll for all employees was approximately \$44.7 million. For the two preceding fiscal years, the Municipality contributed approximately \$2.8 million and \$2.7 million, which represented 100% of required contributions.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

Additional information of ERS is presented in its financial statements for the year ended June 30, 2002, a copy of which can be obtained from the ERS, Minillas Station, PO Box 42003, San Juan, PR 00940.

16. RISK MANAGEMENT

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

17. COMMITMENTS

a. Primary Government

1) Operating Leases

The Municipality leases real property, buildings, vehicles and equipment under several operating lease agreements which generally have terms of one year or less and are automatically renewed for the same terms. Rental expenditures recorded in the basic financial statements for the year ended June 30, 2002, amounted to approximately \$1.7 million. Management believes that the summary of the future minimum rental commitments under noncancelable real property and equipment lease with terms exceeding one year is not significant.

2) Construction

The Municipality had commitments at June 30, 2002 of approximately \$31 million for the construction, improvements, or renovation of several municipal facilities.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

b. Component Units

Port of Ponce

The Port of Ponce is the lessor of certain dock and warehousing facilities. Future minimum rentals receivable under such leases at June 30 2002 are as follows:

2003	\$ 863,311
2004	827,843
2005	827,843
2006	827,843
2007	<u>827,843</u>
Total	<u>\$4,174,683</u>

18. CONTINGENCIES, LIABILITIES FOR CLAIMS AND JUDGMENTS AND OTHER

a. Contingencies and Claims and Judgments against the Municipality

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions. It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial condition of the Municipality.

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 "Reports on Compliance and Internal Control in Accordance with Government Auditing Standards and the Requirements of OMB Circular A-133" for the year ended June 30, 2002, disclosed several material instances of noncompliance with applicable laws and regulations and with internal accounting and administrative controls.

If expenditures are disallowed due to noncompliance with grant programs regulations, the Municipality may be required to reimburse the grantor. Management believes that the Municipality will be able to comply with the terms

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

of corrective action plans that may be requested by the federal grantors. Although, such audits could generate expenditure disallowances under the terms of the grants, management believes that any required reimbursements would not be material.

b. Primary Government Litigations and Claims in Favor of the Municipality

In June 1996, the Ponce Superior Court of the Puerto Rico Court of First Instance entered judgment in favor of the Municipality against several government agencies and the Central Government. Through this judgment, the Court ordered the defendants to construct about 54 projects, which management estimates cost approximately \$160 million, which were included in the Municipal Land Use Plan, and also ordered the defendants to pay the Municipality damages in the amount of \$16.5 million. The parties involved were notified of the judgment on June 26, 1996 and from that date, the amount of the judgment earns interest at 5% annually. The judgment was appealed by all defendants to the Circuit Court and on December 2, 1997 the Circuit Court of Appeals upheld the judgment entered by the Ponce Superior Court. However, the Court modified the damage award and determined that the precise amount of damages to be granted to the Municipality should be determined once the projects covered by the judgment are finished. The Municipality was denied a reconsideration of this determination and appealed to the Supreme court in April 1998 with the purpose of reinstating the damage award. In December 2000, the Supreme Court entered a judgment in favor of the Municipality. Since then, management has been negotiating with the Central Government a work schedule for the realization of the project and the collection of the damages. During 2002, the Municipality received \$9 million related to this case which is included as other revenues in the accompanying basic financial statements.

19. CLOSURE AND POSTCLOSURE CARE COSTS AND LANDFILL OBLIGATIONS

The Municipality owns a landfill, which is used by several municipalities including Ponce and administered by BFI Industries, the landfill administrator, an independent private entity, under an agreement with the Municipality. The Municipality is entitled, under the agreement with the administrator, to certain revenues, principally royalties, resulting from the use of the landfill. In addition, a portion of these revenues is to be deposited in an escrow account to fund the accumulated liability to cover estimated closure and post-closure costs of the landfill. For the year ended June 30, 2002,

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002

revenues earned under the agreement amounted to \$1.8 million and are presented in the accompanying statement of changes in net assets and statement of revenue, expenditures and changes in fund balances. The amounts deposited in the escrow account as part of the agreement with the landfill administrator are presented in the accompanying statement of net assets as cash held in escrow account for landfill closure and post closure care cost. At June 30, 2002 the portion of the revenues required to be deposited in the escrow account was \$3.4 million (same as June 30, 2001).

State and federal laws and regulations require the Municipality to place a final cover on the Municipality's landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for thirty years after closure. In accordance with Statement No. 18 of the "GASB", "Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Costs", the Municipality obtained a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Based on the last study performed in October 2001, as of June 30, 2002 the Municipality recognized approximately \$11 million as the Municipality's estimated obligation for landfill closure and post closure care costs. The estimated amount of \$11 million is based on what it would cost to perform all closure and post closure care in 2002. At June 30, 2002, the percentage of landfill capacity used to date was approximately 68% and the estimated remaining life was approximately 4.7 years.

20. SUBSEQUENT EVENTS

On August 23, 2002, the Government Development Bank for Puerto Rico (GDB) issued \$40,000,000 of revenue bonds to the Municipality of Ponce, authorized by the Municipal Ordinance number 61, Series 2001-2002 and the Resolutions number 7809 and 7794 of the Board Directors of GDB. The proceeds of this loan is to finance improvements to the Port of Ponce and to cancel a loan of \$2,000,000.

The principal and interest of this loan will be paid by future revenues from the operations of Port of Ponce, and if it is necessary, it will be paid with the withholdings over the Basic Contribution of the Municipality. The CRIM will withheld from the monthly payments to the Municipality the amount necessary to cover such payments.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF PONCE
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2002**

The annual interest rate for the revenue bonds will not exceed 12%. Otherwise, it will accumulate interest over a variable interest rate revised in October 1, January 1, April 1, and July 1 every year until the bonds are sold.

COMBINING SCHEDULES

MUNICIPALITY OF PONCE

General Fund

Comparative Balance Sheet

June 30, 2002 and 2001

Assets	<u>2002</u>	<u>2001</u>
Cash and cash equivalents	\$ 5,836,880	\$ 4,955,530
Cash with fiscal agent	3,000,000	
Accounts receivable :		
Municipal license tax		201,390
Intergovernmental		231,078
Due from other governmental entities		1,334,017
Advances to other funds	342,577	447,479
Restricted assets :		
Cash with fiscal agent	31,000,766	36,626,726
Cash held in escrow account for landfill closure and postclosure care costs	<u>3,403,668</u>	<u>3,400,000</u>
Total assets	<u><u>\$43,583,891</u></u>	<u><u>\$47,196,220</u></u>
Liabilities		
Accounts payable and accrued liabilities	\$ 11,213,276	\$ 7,749,634
Due to component unit		270,820
Due to other agencies	582,995	
Advances from other funds	2,620,858	3,390,306
Deferred municipal license tax revenues	<u>14,428,134</u>	<u>13,480,504</u>
Total liabilities	<u>28,845,263</u>	<u>24,891,264</u>
Fund Balance		
Reserved for :		
Encumbrances	99,004	298,304
Advances	342,577	447,479
Landfill closure and postclosure care costs	3,400,000	3,400,000
Capital projects	31,000,766	38,419,109
Unreserved fund balance (deficiency)	<u>(20,103,719)</u>	<u>(20,259,936)</u>
Total fund balance	<u>14,738,628</u>	<u>22,304,956</u>
Total liabilities and fund balance	<u><u>\$43,583,891</u></u>	<u><u>\$47,196,220</u></u>

MUNICIPALITY OF PONCE

General Fund

**Comparative Statements of Revenues,
Expenditures and Changes in Fund Balance**

Years ended June 30, 2002 and 2001

	2002	2001
Revenues :		
Property taxes	\$ 31,047,148	\$ 30,525,867
Municipal license tax	16,927,289	17,207,104
Royalties and other	1,816,746	1,836,061
Licenses and permits	3,284,751	2,303,993
Charges for service and rents	563,349	254,921
Intergovernmental revenues - State Contributions	9,141,848	7,479,839
Interests, fines and penalties	2,040,484	1,171,742
Other revenues	16,193,370	1,183,293
Total revenues	\$ 81,014,985	\$ 61,962,820
Expenditures :		
General government	29,712,061	23,850,734
Public safety	8,979,368	6,405,239
Public works	16,490,889	14,355,530
Culture and recreation	7,510,837	6,710,750
Health and welfare	10,779,890	10,687,796
Legal services	852,146	750,619
Capital outlays	11,478,985	8,057,043
Debt service :		
Principal retirement	3,910,558	3,677,423
Interest and other	1,082,302	1,846,544
Total expenditures	90,797,036	76,341,678
Deficiency of revenues under expenditures	(9,782,051)	(14,378,858)
Other financing sources (uses) :		
Transfers to component unit		(315,000)
Operating transfers from other funds	215,723	470,858
Proceeds from Municipal Finance Agency		714,993
Loan proceeds	2,000,000	31,765,000
Total other financing sources	2,215,723	32,635,851
Excess (Deficiency) of revenues over (under) expenditures and other financing sources (uses)	(7,566,328)	18,256,993
Fund Balance at beginning of year	22,304,956	4,047,963
Fund Balance at end of year	\$ 14,738,628	\$ 22,304,956

MUNICIPALITY OF PONCE
Combining Balance Sheet
Nonmajor Governmental Funds
June 30, 2002

ASSETS

	Home Devolutions	Ryan White	F.E.M.A.	Program Income Quality Health	Local law	San Anton	Total Nonmajor Governmental Funds
Cash and cash equivalent	\$ 184,507	\$ 389	\$ 16,087	\$ 7,883	\$ 344,329	\$ 106,540	\$ 659,735
Federal grant receivable		275,627	740,096				1,015,723
Total assets	\$ 184,507	\$ 276,016	\$ 756,183	\$ 7,883	\$ 344,329	\$ 106,540	\$ 1,675,458

LIABILITIES:

Account payable	\$ -	\$ 215,141	\$ 437,649	\$ -	\$ -	\$ -	\$ 652,790
Due to general fund		818	318,534				319,352
Due to federal government	184,507	51,757	-	10	344,329	106,540	687,143
Total liabilities	\$ 184,507	\$ 267,716	\$ 756,183	\$ 10	\$ 344,329	\$ 106,540	\$ 1,659,285

FUND BALANCE:

Federal programs		8,300		7,873			16,173
Total fund balances	-	8,300	-	7,873	-	-	16,173
Total liabilities and fund balance	\$ 184,507	\$ 276,016	\$ 756,183	\$ 7,883	\$ 344,329	\$ 106,540	\$ 1,675,458

MUNICIPALITY OF PONCE
Combining Statement of Revenues, Expenditures and Changes in Fund Balances
Nonmajor Governmental Funds
June 30, 2002

	<u>Home Devolutions</u>	<u>Ryan White</u>	<u>F.E.M.A.</u>	<u>Program Income Quality Health</u>	<u>Local law</u>	<u>San Anton</u>	<u>Total Nonmajor Governmental Funds</u>
Federal grants	\$ -	\$ 2,183,157	\$ -	\$ -	\$ -	\$ -	\$ 2,183,157
Expenditures	<u>-</u>	<u>2,183,157</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,183,157</u>

Municipality of Ponce
Capital Assets Used in the Operation of Governmental Funds
Schedule of Changes By Function and Activity
For the fiscal year ended June 30, 2002

Governmental funds capital assets:	2002	2001
Land	\$ 24,439,718	\$ 24,327,718
Buildings	77,599,714	77,546,609
Improvements other than buildings	4,357,261	4,339,196
Machinery and equipment	13,223,402	12,591,524
Infrastructure	43,320,459	42,520,663
Construction in progress	22,822,121	7,611,428
Total governmental funds capital assets	\$ 185,762,675	\$ 168,937,138
Investment in governmental funds capital asset by sources		
General fund	\$ 65,833,560	\$ 60,008,023
Special revenue fund	72,500,000	72,500,000
Capital projects funds	47,429,115	36,429,115
Total governmental funds capital assets	\$ 185,762,675	\$ 168,937,138

PART III. STATISTICAL SECTION

MUNICIPALITY OF PONCE

General Governmental
Revenues by Source¹

Last Ten Fiscal Years

	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1994</u>	<u>1993</u>
Revenues by Sources:										
Property taxes	\$ 43,025,904	\$ 39,249,194	\$ 37,931,306	\$ 34,482,178	\$ 35,988,513	\$ 34,343,273	\$ 34,007,003	\$ 36,156,874	\$ 32,401,543	\$ 25,486,486
Sale of property tax collection rights	-	-	-	6,963,764	-	-	-	-	-	-
Municipal license taxes	16,927,289	17,207,104	14,629,789	14,712,311	13,368,317	12,266,161	11,630,296	11,014,586	7,402,057	7,205,700
Royalties and others	1,816,746	1,836,061	2,270,209	2,611,715	1,691,365	1,608,064	1,449,478	-	-	-
Licenses and permits	3,284,751	2,303,993	3,794,226	2,922,294	3,066,209	2,349,751	2,425,462	679,398	526,013	647,431
Changes for services and rent	563,349	254,921	337,499	311,889	435,124	380,742	426,547	411,650	195,191	236,336
Intergovernmental:										
Federal	42,450,395	42,903,341	37,247,396	33,844,882	41,148,100	40,235,834	37,169,071	33,842,656	31,812,543	33,388,257
State contributions	9,141,848	7,479,839	5,893,338	9,436,035	9,526,562	10,284,877	8,375,676	14,152,157	8,503,021	19,010,479
Interest, fines and penalties	2,189,785	1,607,403	1,846,508	1,201,096	1,522,108	1,029,154	824,931	760,390	427,321	667,003
Miscellaneous	16,193,370	1,183,293	1,277,055	881,891	967,384	855,628	197,308	1,337,323	788,978	1,970,134
Total	\$ 135,593,437	\$ 114,025,149	\$ 105,227,326	\$ 107,368,055	\$ 107,713,682	\$ 103,353,484	\$ 96,505,772	\$ 98,355,034	\$ 82,056,667	\$ 88,611,826

¹Includes General, Special Revenue, Debt Service and Capital Projects funds.

MUNICIPALITY OF PONCE

**General Governmental
Expenditures by Function¹**

Last Ten Fiscal Years

	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1994</u>	<u>1993</u>
General government	\$ 29,712,061	\$ 23,850,734	\$ 25,486,551	\$ 28,112,874	\$ 24,512,771	\$ 24,131,708	\$ 27,709,822	\$ 22,826,460	\$ 22,237,695	\$ 22,862,784
Public safety	8,979,368	7,589,077	6,982,414	6,413,669	6,671,964	6,227,773	4,861,324	4,170,426	3,436,412	3,660,208
Public work	16,490,889	14,355,530	13,147,209	15,365,484	14,624,163	16,207,159	22,692,792	14,982,726	9,439,458	16,026,679
Culture and recreation	7,510,837	6,710,750	6,339,466	6,153,458	6,591,802	7,206,742	5,712,616	3,775,274	3,163,318	4,795,706
Health and welfare	25,970,381	33,034,986	30,662,745	25,652,794	27,351,346	28,000,998	26,363,720	23,591,668	20,684,411	20,289,454
Urban development	16,648,032	5,798,916	4,605,672	3,811,503	11,547,293	12,724,744	11,492,981	18,410,291	12,223,450	13,154,184
Legal service	852,146	750,619	729,740	656,729	768,987	757,750	999,848	640,904	525,401	790,663
Education	10,651,201	9,557,394	7,186,080	6,860,854	6,326,416	5,176,759	4,960,151	5,529,230	4,840,674	6,534,644
Capital outlays	11,478,985	8,057,043	4,691,037	1,568,265	3,586,421	2,381,098	1,358,908	1,898,839	5,727,501	14,009,900
Debt service:										
Principal	9,270,558	11,127,423	10,493,729	13,488,587	11,901,156	9,337,782	4,325,740	14,563,796	2,925,000	10,706,885
Interest and other	5,889,765	6,951,417	7,363,307	8,253,395	8,243,261	7,330,738	7,199,025	6,374,151	2,248,135	1,710,179
Total expenditure	<u>\$ 143,454,223</u>	<u>\$ 127,783,889</u>	<u>\$ 117,687,950</u>	<u>\$ 116,337,612</u>	<u>\$ 122,125,580</u>	<u>\$ 119,483,251</u>	<u>\$ 117,676,927</u>	<u>\$ 116,763,765</u>	<u>\$ 87,451,455</u>	<u>\$ 114,541,286</u>

¹Includes General, Special Revenue, Debt Service and Capital Projects funds.

MUNICIPALITY OF PONCE

Assessed Value of Taxable Real and Personal Property¹

Last Five Years

<u>Fiscal Year</u>	<u>Gross Valuation</u>	<u>Exempt Value</u>	<u>Exonerated Value</u>	<u>Net Assessed Value</u>
2002	\$ 1,018,613,365	\$ 192,390,599	\$ 248,432,894	\$ 577,789,872
2001	978,908,362	185,078,640	237,675,408	556,154,314
2000	973,876,077	208,745,237	240,065,346	525,065,494
1999	966,180,410	220,666,139	243,445,394	502,068,877
1998	951,365,226	214,428,035	239,388,477	497,548,714

Source: Municipal Revenue Collection Center.

¹ Information prior to 1998 is unavailable.

MUNICIPALITY OF PONCE

Real and Personal Property Tax Levies and Collections¹

Last Five Fiscal Years

<u>Fiscal Year</u>	<u>Total Current Year Tax Levy</u>	<u>Current Tax Collected</u>	<u>Percent of Levy Collected</u>	<u>Delinquent Tax Collected</u>	<u>Total Tax Collected</u>	<u>Total Tax Collected as % of Current Levy</u>
2002	\$ 42,247,108	\$ 32,926,019	78%	\$ 3,350,277	\$ 36,276,296	86%
2001	40,726,482	31,744,908	78%	3,458,559	35,203,467	86%
2000	38,247,404	33,614,781	88%	3,363,026	36,977,807	97%
1999	36,618,181	29,287,336	80%	3,384,112	32,671,447	89%
1998	35,594,733	28,673,887	81%	5,281,537	33,955,424	95%

Source: Municipal Revenue Collection Center.

¹ Information prior to 1998 is unavailable.

MUNICIPALITY OF PONCE

Property Tax Rates

Last Ten Fiscal Years

Real Property

<u>Fiscal Year</u>	<u>General Purpose¹</u>	<u>Bond Redemption²</u>	<u>Commonwealth of Puerto Rico³</u>	<u>Discount^a</u>	<u>Total</u>
2002	4.00%	1.50%	1.03%	0.20%	6.73%
2001	4.00%	1.50%	1.03%	0.20%	6.73%
2000	4.00%	1.50%	1.03%	0.20%	6.73%
1999	4.00%	1.50%	1.03%	0.20%	6.73%
1998	4.00%	1.50%	1.03%	0.20%	6.73%
1997	4.00%	1.25%	1.03%	0.20%	6.48%
1996	4.00%	1.25%	1.03%	0.20%	6.48%
1995	4.00%	1.25%	1.03%	0.20%	6.48%
1994	4.00%	1.25%	1.03%	0.20%	6.48%
1993	4.00%	1.25%	1.03%	0.20%	6.48%

¹Represents the Municipality's basic property tax rate which is appropriated for general purposes.

²Represents the ad valorem tax restricted for Debt Service.

³Represents a percentage retained by Commonwealth of Puerto Rico.

^aRepresents amount by the Commonwealth of Puerto Rico.

MUNICIPALITY OF PONCE

Property Tax Rates

Last Ten Fiscal Years

Personal Property

<u>Fiscal Year</u>	<u>General Purpose¹</u>	<u>Bond Redemption²</u>	<u>Commonwealth of Puerto Rico³</u>	<u>Discount⁴</u>	<u>Total</u>
2002	6.00%	1.50%	1.03%	0.20%	8.73%
2001	6.00%	1.50%	1.03%	0.20%	8.73%
2000	6.00%	1.50%	1.03%	0.20%	8.73%
1999	6.00%	1.50%	1.03%	0.20%	8.73%
1998	6.00%	1.50%	1.03%	0.20%	8.73%
1997	6.00%	1.25%	1.03%	0.20%	8.48%
1996	6.00%	1.25%	1.03%	0.20%	8.48%
1995	6.00%	1.25%	1.03%	0.20%	8.48%
1994	6.00%	1.25%	1.03%	0.20%	8.48%
1993	6.00%	1.25%	1.03%	0.20%	8.48%

¹Represents the Municipality's basic property tax rate which is appropriated for general purposes.

²Represents the ad valorem tax restricted for Debt Service.

³Represents a percentage retained by Commonwealth of Puerto Rico.

⁴Represents amount by the Commonwealth of Puerto Rico.

MUNICIPALITY OF PONCE

Computation of Legal Debt Margin

June 30,2002
(in thousands of dollars)

Assessed value of property located within the Municipality of Ponce	<u>\$ 826,222</u>
Legal debt limit- 10% of the total assessed value of property located within The Municipality of Ponce	\$ 82,622
Total general obligation bond outstanding applicable to legal debt limit	<u>(75,345)</u>
Available legal margin	<u>\$ 7,277</u>
Ratio of available legal debt margin to legal debt limit	<u>8.81%</u>

Sources: Assessed property value was provided by the Municipal Revenue Collection Center.

MUNICIPALITY OF PONCE

Ratio of Net General Bonded Debt To Assessed Value and Net Bonded Debt per Capita

Last Ten Fiscal Years

(In thousands of dollars)

<u>Fiscal Year</u>	<u>Population</u>	<u>Assessed Value</u>	<u>Gross Bonded Debt</u>	<u>Less Debt Service Fund Balance</u>	<u>Net Bonded Debt</u>	<u>Ratio of Net Bonded Debt to Assessed Value</u>	<u>Net Bonded Debt per Capital</u>
2002	187,935	\$ 826,222	\$ 154,864	\$ 8,663	\$ 146,201	0.18	\$ 0.778
2001	186,925	838,689	195,812	6,918	188,894	0.23	1.011
2000	186,475	765,130	174,760	6,788	167,972	0.22	0.901
1999	193,640	745,514	167,634	5,926	161,708	0.22	0.835
1998	191,469	725,285	135,085	8,314	126,771	0.17	0.662
1997	189,900	725,703	130,528	9,212	121,316	0.17	0.639
1996	189,988	601,479	121,640	9,737	111,903	0.19	0.589
1995	188,722	690,167	125,972	7,006	118,966	0.17	0.630
1994	193,069	a	119,430	8,291	111,139	a	0.576
1993	193,053	a	102,261	7,595	94,666	a	0.490

Source: ¹ U.S. Bureau of the Census.

² Municipal Revenue Collection Center.

Information is unavailable.

MUNICIPALITY OF PONCE

**Ratio of Annual Debt Service for General Bonded Debt
to Total General Governmental Expenditures**

Last Ten Fiscal Years
(in thousands of dollar)

	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1994</u>	<u>1993</u>
Debt service:										
Principal	\$ 5,360	\$ 4,950	\$ 2,245	\$ 6,685	\$ 5,130	5,045	2,245	2,115	2,925	\$ 10,706
Interest	4,807	3,608	2,766	2,940	3,373	2,724	2,766	2,743	2,248	1,710
Total debt service	10,167	8,558	5,011	9,625	8,503	7,769	5,011	4,858	5,173	12,416
Total general expenditures ¹	\$ 143,454	\$ 127,783	\$ 117,687	\$ 116,337	\$ 122,125	119,483	117,676	116,763	87,451	\$ 114,541
Debt services to general expenditures (percentage)	<u>7.09%</u>	<u>6.70%</u>	<u>4.26%</u>	<u>8.27%</u>	<u>6.96%</u>	<u>6.50%</u>	<u>4.26%</u>	<u>4.16%</u>	<u>5.92%</u>	<u>10.84%</u>

¹ Includes General, Special Revenue, Debt Service and Capital Projects funds.

MUNICIPALITY OF PONCE

Construction and Bank Deposits For the Last Ten Fiscal Years

Calendar Year	<u>Commercial Construction</u>		<u>Residential Construction</u>		<u>Bank Deposits</u>
	<u>Square Feet of Site Approved</u>	<u>Value</u>	<u>Square Feet of Site Approved</u>	<u>Value</u>	
2002	1,397,322	\$ 19,288,812	698,171	\$ 32,542,838	\$ 627,548,067
2001	301,088	17,907,729	1,607,473	11,456,040	574,313,637
2000	42,551	43,807,905	133,572	14,634,427	559,161,303
1999	63,088	25,847,625	36,010	10,229,560	523,190,402
1998	75,081	21,490,692	58,863	9,181,875	451,025,760
1997	389,536	21,190,842	52,231	19,546,431	399,266,148
1996	380,290	11,648,366	52,709	10,042,513	356,247,625
1995	37,772	11,638,545	97,841	3,402,791	255,944,779
1994	189,551	1,826,922	29,089	5,280,280	208,237,779
1993	32,805	6,871,250	654,702	9,922,925	179,351,393

Sources: Puerto Rico Planning Board for the years 1993 to 1997.

Municipal license Tax and Permits offices of the Municipality
of Ponce for the years 1998 to 2002.

COMMENTS RELATIVE TO STATISTICAL SECTION

The following statistical tables that are recommended for inclusion by the Governmental Accounting Standards Board are not included for the reasons stated below:

- Assessed and Estimated Actual Value of Taxable Property – Last Ten fiscal Years –Municipality has not estimated the actual value of real property since 1957.
- Special Assessment Collections – Last Ten Fiscal Years – Municipality has had no special assessments for the past ten years.
- Principal Taxpayers – This information is confidential and protected by law.

MUNICIPALITY OF PONCE

Demographic Statistics

For the Last Ten Fiscal Years

<u>Fiscal Year</u>	<u>Population</u>	<u>Employment</u>	<u>Unemployment Rate</u>
2002	187,935	56,355	12.30%
2001	186,925	53,212	12.30%
2000	186,475	53,336	12.30%
1999	193,640	51,683	13.00%
1998	191,469	50,856	14.97%
1997	189,900	50,835	16.53%
1996	189,988	50,754	16.45%
1995	188,722	49,736	15.99%
1994	193,069	48,222	16.50%
1993	193,053	48,123	19.63%

Sources: U.S. Bureau of the Census.

Population Density

	<u>Square Miles</u>	<u>Population per Square Mile</u>
Ponce	187.94	992.20

Population Age Distribution as of 2000 Census

<u>0-14</u>	<u>15-24</u>	<u>25-44</u>	<u>45-64</u>	<u>65+</u>
45,203	32,228	48,225	39,169	21,650

Sources: U.S. Bureau of the Census.