

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

**MUNICIPIO DE QUEBRADILLAS  
AUDITORÍA 2009-2010  
30 DE JUNIO DE 2010**

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS**

**BASIC FINANCIAL STATEMENTS  
FOR THE FISCAL YEAR ENDED  
JUNE 30, 2010**

**ORTIZ, RIVERA, RIVERA & CO.**

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

Suite 152, PO Box 70250, San Juan, P.R. 00936-7250 • Phone (787) 756-8524, Fax (787) 274-0562

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF QUEBRADILLAS**  
**BASIC FINANCIAL STATEMENTS**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**TABLE OF CONTENTS**

	<u>Pages</u>
<b>PART I - FINANCIAL SECTION</b>	
Independent Auditors' Report.....	1-2
Management's Discussion and Analysis .....	3-9
Basic Financial Statements:	
Government-Wide Financial Statements:	
Statement of Net Assets .....	10
Statement of Activities.....	11
Fund Financial Statements-Governmental Funds	
Balance Sheet .....	12-13
Reconciliation of the Governmental Funds Balance Sheet to Statement of Net Assets.....	14
Statement of Revenues, Expenditures, and Changes in Fund Balances .....	15
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balance of Governmental Funds to the Statement of Activities .....	16
Statement of Revenues and Expenditures - Budget and Actual - General and Debt Service Funds .....	17
Notes to Basic Financial Statements .....	18-45

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**TABLE OF CONTENTS (CONTINUED)**

	<u>Pages</u>
<b>PART II – SINGLE AUDIT SECTION</b>	
Schedule of Expenditures of Federal Awards .....	46
Notes to Schedule of Expenditures of Federal Awards .....	47
Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards .....	48-49
Independent Auditor's Report on Compliance with Requirements that could have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance in accordance with OMB Circular A-133 .....	50-52
Schedule of Findings and Questioned Costs .....	53
Schedule of Status of Prior Year Audit Findings and Questioned Costs .....	54-55

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## INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Quebradillas, as of and for the year ended June 30, 2010, which collectively comprise the Municipality's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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. 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Quebradillas as of June 30, 2010, and the respective changes in financial position, thereof and the respective budgetary comparison for the general and debt service funds for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 18, 2010 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations,

contracts and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtain during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Quebradillas's financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

San Juan, Puerto Rico  
October 18, 2010

*Ortiz, Rivera, Rivera & Co.*

The stamp 2571458 was affixed  
to the original of this report.



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**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

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***MANAGEMENT'S DISCUSSION AND ANALYSIS***

The Municipality of Quebradillas (the "Municipality") discussion and analysis has been designed with the followings goals:

- a) Assist the reader in focusing on significant financial issues,
- b) Provide an overview of the Municipality's financial activity,
- c) Identify changes in the Municipality's financial position (its ability to address the next and subsequent year challenges),
- d) Identify any material deviations from the financial plan (the approved budget), and;
- e) Identify individual fund issues or concerns.

Since the Management's Discussion and Analysis (MD & A) is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the Municipality's financial statements.

***FINANCIAL HIGHLIGHTS***

- The Municipality net assets increased by \$2,228,661.
- In the fund financial statements, general fund revenues increased \$733,424 (or 7%).
- The General Fund (the primary operating fund) reflected, on a current financial resource basis, an increase of \$394,019.
- On a budgetary basis, actual revenues exceed actual expenditures by \$499,303.
- Capital expenditures amounted to \$1,544,792.

***USING THIS ANNUAL REPORT***

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

***Government-Wide Financial Statements***

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

**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

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

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

**Fund Financial Statements**

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

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

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

**Infrastructure Assets**

Historically, a government's largest group of assets (infrastructure – roads, bridges, traffic signals, underground pipes [unless associated with a utility], etc.) have not been reported nor

**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

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depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a)

Depreciate these assets over their estimated useful life or (b) Develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach), which periodically (at least every third year), by category, measures and demonstrates its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time. The Municipality has elected to depreciate infrastructure assets instead of using the modified approach.

## **FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE**

### **Net Assets**

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The Municipality's net assets totaled \$24.7 million at the end of 2010, compared to \$22.5 million at the end of the previous year.

The largest portion of the Municipality's net assets consists of the investment made throughout the years in capital assets such as land, buildings, equipment and infrastructure. The Municipality uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although, the Municipality's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from the Debt Service Fund, since the capital assets themselves cannot be used to liquidate these liabilities. The amounts restricted for debt service represents another portion of the net assets, and these are resources subject to external restrictions for the purposes explained above.

The unrestricted deficit is the consequence of previous budgets which did not provide funding for incurred long-term obligations such as compensated absences and claims and judgments among others. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation. Consequently, the Municipality cannot draw from its existing assets to provide services to its citizens and depends on its taxing ability to continue its operations. The restricted portion consists of monies reserved for debt service and future capital expenditures.

**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

**Municipality of Quebradillas  
Condensed Statement of Net Assets  
June 30, 2010 and 2009**

	<u>2010</u>	<u>2009</u>
Current assets	\$ 8,462,536	\$ 7,082,277
Capital assets	30,649,190	29,971,997
Total assets	<u>39,111,726</u>	<u>37,054,274</u>
Current liabilities	3,353,923	3,876,164
Noncurrent liabilities	10,976,503	10,625,471
Total liabilities	<u>14,330,426</u>	<u>14,501,635</u>
Invested in capital assets, net of related debt	30,649,190	29,971,997
Restricted	1,288,825	1,180,500
Unrestricted	(7,156,715)	(8,599,858)
Total net assets	<u>\$ 24,781,300</u>	<u>\$ 22,552,639</u>

**Changes in Net Assets**

The Municipality's net assets increased by \$2.1 million approximately, thirty- two (32%) percent of the Municipality's total revenue came from Taxes generated by the general fund. Federal Grants was fifteen (15%) percent, while the State Contributions made fifty (50%) percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for general government, public works and health and welfare.

**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

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**FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS**

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

**Governmental Funds**

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$5,368,613 an increase of \$1,907,500 in comparison with the prior year. There are reservations of fund balance amounting to \$1,347,455.

The general fund is included within the governmental funds; it is the chief operating fund of the Municipality. As of June 30, 2010, the general fund has a balance of \$568,233. The prior year superavit of \$174,214 was increased by \$394,019 during fiscal year 2010.

**GENERAL FUND BUDGETARY HIGHLIGHTS**

Over the course of the year, the Municipality Council revised the Municipality's budget to reclassify certain expenditures among the different governmental functions. Such reclassifications were necessary to provide for the developments that affected the Municipality's finances.

Revenues of the current year had increased by \$733,424 compared with the prior year. The increase in fund balance is directly related to this increase in revenues. The actual revenues exceeded the revised budget revenues by \$62,820 (net). The most significant variances were in municipal licenses and sales taxes by \$170,696 and \$63,285, respectively.

**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

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**CAPITAL ASSETS AND DEBT ADMINISTRATION**

**Capital Assets**

The Municipality's investment in capital assets as of June 30, 2010, amounts to \$39.3 million, net of accumulated depreciation of \$8.7 million, leaving a net book value of \$30.1 million. This investment in capital assets includes land, buildings, improvements, equipment, intangibles, infrastructure and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond issuances. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes.

The Municipality acquired a total of \$2,088,726 of capital assets during the fiscal year 2009-2010. Capital assets acquired during the year were as follows:

- Construction in Progress - \$727,034
- Building and building improvements - \$654,634
- Acquisition of Equipment and Vehicles - \$557,621

Other projects related to repair and maintenance of roads (not capitalized) was development during the year 2010.

**Debt Administration**

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

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

**Commonwealth of Puerto Rico  
Municipality of Quebradillas**

**Management's Discussion and Analysis**

**Year Ended June 30, 2010**

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as projected by GDB, will be sufficient to service to maturity the municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

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

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

The Municipality relies primarily on property and municipal taxes as well as federal grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal grant revenues may vary if new grants are available but the revenue also is very predictable.

**FINANCIAL CONTACT**

The Municipality's financial statements are designed to present users (citizens, taxpayers, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact Mrs. Edna M Perez, Chief Financial Officer on the Finance Offices in the Central Town, Quebradillas, Puerto Rico.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
STATEMENT OF NET ASSETS  
JUNE 30, 2010**

<u>Assets</u>	<u>Governmental Activities</u>
Cash in bank (Notes 2 and 5)	\$ 2,919,019
Cash with fiscal agent (Notes 2 and 5)	3,342,460
Accounts receivable:	
Sales and use taxes	63,764
Property taxes	76,850
Due from other agencies (Note 9)	2,060,443
Capital assets, net (Note 11)	<u>30,649,190</u>
 Total assets	 <u><u>\$ 39,111,726</u></u>
 <b><u>Liabilities and Net Assets</u></b>	
<b>Liabilities</b>	
Accounts payable and accrued liabilities	\$ 644,321
Due to other agencies (Note 12)	1,967,034
Matured bonds and interest payable	300,498
Deferred revenues (Note 13):	
Municipal license tax	442,070
Noncurrent liabilities (Note 15):	
Due within one year	563,345
Due in more than one year	9,961,999
Accrued interest	451,159
Total liabilities	<u>14,330,426</u>
<b>Net Assets</b>	
Investment in capital assets, net of related debt	30,649,190
Restricted for:	
Debt service	1,288,825
Unrestricted	<u>(7,156,715)</u>
Total net assets	<u>24,781,300</u>
 Total liabilities and net assets	 <u><u>\$ 39,111,726</u></u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
STATEMENT OF ACTIVITIES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

<u>Functions/Programs</u>	Program Revenues			Net (Expense) Revenue and Changes in Net Assets Primary
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
				Governmental Activities
<b>Primary Government:</b>				
General government	\$ 6,002,688	\$ 402,137	\$ -	\$ (5,600,551)
Public safety	1,799,805			(1,799,805)
Culture and recreation	565,156			(565,156)
Health and welfare	946,055	585,235		(360,820)
Public work	1,829,457		689,871	(1,139,586)
Economic development	248,436			(248,436)
Interest on long-term debt	324,431			(324,431)
Total primary government	\$ 11,716,028	\$ 402,137	\$ 585,235	\$ 689,871
				(10,038,785)
				2,496,923
				690,378
				1,256,215
				6,068,433
				40,024
				1,590,789
				12,142,762
				2,103,977
				22,677,323
				\$ 24,781,300
				2,496,923
				690,378
				1,256,215
				6,068,433
				40,024
				1,590,789
				12,142,762
				2,103,977
				22,677,323
				\$ 24,781,300

General revenues:

Property taxes (Note 6)	2,496,923
Municipal license tax (Note 7)	690,378
Sales and use tax (Note 8)	1,256,215
Grants and contributions not restricted to specific programs	6,068,433
Interest, fines and penalties	40,024
Miscellaneous	1,590,789
Total general revenues	12,142,762
Change in net assets	2,103,977
Net assets at beginning of year as restated (Note 21)	22,677,323
Net assets at end of year	\$ 24,781,300

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

COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
BALANCE SHEET-GOVERNMENTAL FUNDS  
JUNE 30, 2010

<u>Assets</u>	<u>General</u>	<u>Debt Service</u>	<u>SBGP Program</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Cash and cash equivalents (Notes 2 and 5)	\$ 1,450,710	\$ -	\$ 5,703	\$ 1,462,606	\$ 2,919,019
Cash with fiscal agent (Notes 2 and 5)		1,512,473		1,829,987	3,342,460
Accounts receivable:					
Sales and use taxes	63,764				63,764
Property taxes		76,850			76,850
Due from other agencies (Note 9)	1,949,509		54,191	56,743	2,060,443
Due from other funds (Note 10)	184,694			438,868	623,562
 Total assets	 <u>\$ 3,648,677</u>	 <u>\$ 1,589,323</u>	 <u>\$ 59,894</u>	 <u>\$ 3,788,204</u>	 <u>\$ 9,086,098</u>

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

-12-

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COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
BALANCE SHEET-GOVERNMENTAL FUNDS  
JUNE 30, 2010

<u>Liabilities and Fund Balance (Deficit)</u>	<u>General</u>	<u>Debt Service</u>	<u>SBGP Program</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
<b>Liabilities</b>					
Accounts payable and accrued liabilities	\$ 235,572	\$ -	\$ 93,422	\$ 55,327	\$ 384,321
Due to other funds (Note 10)	438,814		74,454	110,294	623,562
Due to other agencies (Note 12)	1,963,988			3,046	1,967,034
General obligations: (Note 15)					
Bonds		220,000			220,000
Interest		80,498			80,498
Deferred revenues: (Note 13)					
Municipal license tax	442,070				442,070
Total liabilities	<u>3,080,444</u>	<u>300,498</u>	<u>167,876</u>	<u>168,667</u>	<u>3,717,485</u>
<b>Fund Balances (Deficit)</b>					
Reserved for:					
Encumbrances	58,630				58,630
Debt service		1,288,825			1,288,825
Unreserved fund balance (deficit)	509,603		(107,982)	3,619,537	4,021,158
Total fund balance (deficit)	<u>568,233</u>	<u>1,288,825</u>	<u>(107,982)</u>	<u>3,619,537</u>	<u>5,368,613</u>
Total liabilities and fund balance (deficit)	<u>\$ 3,648,677</u>	<u>\$ 1,589,323</u>	<u>\$ 59,894</u>	<u>\$ 3,788,204</u>	<u>\$ 9,086,098</u>

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

-13-

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
RECONCILIATION OF THE GOVERNMENTAL FUNDS  
BALANCE SHEET TO STATEMENT OF NET ASSETS  
JUNE 30, 2010**

Total fund balances - governmental funds \$ 5,368,613

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

- Capital assets, net used in governmental activities are not current financial resources and therefore are not reported in the governmental funds balance sheet 30,649,190
  
- Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds. **(Note 4)** (11,236,503)

Net assets of governmental activities \$ 24,781,300

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

-14-  
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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

	<u>General</u>	<u>Debt Service</u>	<u>SBG Program</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
<b>REVENUES</b>					
Property taxes (Note 6)	\$ 1,911,333	\$ 585,590	\$ -	\$ -	\$ 2,496,923
Municipal license taxes (Note 7)	690,378				690,378
Sales and use taxes (Note 8)	851,462	404,753			1,256,215
Licenses, permits, and other local taxes	363,905				363,905
Charges for services	38,232				38,232
<b>Intergovernmental revenues (Note 14):</b>					
Federal grants and contributions	5,350,400		689,871	585,235	1,275,106
State contributions	39,312	712		718,033	6,068,433
Interest, fines, and penalties	1,584,590				40,024
Other revenues	10,829,612	991,055	689,871	6,199	1,590,789
Total revenues				<u>1,309,467</u>	<u>13,820,005</u>
<b>EXPENDITURES</b>					
Current:					
General government	5,699,120			185,047	5,884,167
Public safety	1,735,512			18,120	1,753,632
Health and welfare	520,014			426,041	946,055
Culture and recreation	266,183			216,343	482,526
Public works	1,171,094				1,171,094
Economic development			213,576	34,860	248,436
Capital outlays	234,597		587,140	723,055	1,544,792
Debt service:					
Principal		1,800,641			1,800,641
Interest and other		311,162			311,162
Total expenditures	<u>9,626,520</u>	<u>2,111,803</u>	<u>800,716</u>	<u>1,603,466</u>	<u>14,142,505</u>
Excess (deficiency) of revenues over (under) expenditures	<u>1,203,092</u>	<u>(1,120,748)</u>	<u>(110,845)</u>	<u>(293,999)</u>	<u>(322,500)</u>
<b>OTHER FINANCING SOURCES (USES)</b>					
Loan proceeds	420,000				2,230,000
Transfers in	540,293	1,769,366		1,810,000	2,309,659
Transfers out	(1,769,366)	(540,293)			(2,309,659)
Total other financing sources (uses)	<u>(809,073)</u>	<u>1,229,073</u>	<u>-</u>	<u>1,810,000</u>	<u>2,230,000</u>
Excess (deficiency) of revenues over (under) expenditures and other financing sources	394,019	108,325	(110,845)	1,516,001	1,907,500
<b>FUND BALANCE AT BEGINNING OF YEAR</b>	174,214	1,180,500	2,863	2,103,536	3,461,113
<b>FUND BALANCE (DEFICIT) AT END OF YEAR</b>	<u>\$ 568,233</u>	<u>\$ 1,288,825</u>	<u>\$ (107,982)</u>	<u>\$ 3,619,537</u>	<u>\$ 5,368,613</u>

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12

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
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, 2010**

Net change in fund balances - total governmental funds	\$ 1,907,500
Amounts reported for governmental activities in the statement of activities are different because:	
• Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.	1,544,792
• 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.	(867,599)
• Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the fund financial statements.	(2,230,000)
• 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.	1,800,641
• Change in accrued interest expense which does not require the use of current financial resources.	(13,269)
• 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.	<u>(38,088)</u>
Changes in net assets of governmental activities	<u><u>\$2,103,977</u></u>

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
STATEMENT OF REVENUES AND EXPENDITURES, BUDGET AND ACTUAL - GENERAL AND DEBT SERVICE FUNDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

	General Fund			Debt Service Fund			Variance with Final Budget-Positive (Negative)
	Budgeted Amounts Original	Final	Actual	Budgeted Amounts Original	Final	Actual	
<b>REVENUES</b>							
Property taxes	\$ 1,898,363	\$ 1,898,363	\$ 1,899,946	\$ 527,362	\$ 527,362	\$ 585,590	\$ 58,228
Municipal license taxes	500,000	500,000	670,696				170,696
Sales taxes	790,000	1,064,004	1,127,289				63,285
Licenses and permits	581,000	581,000	332,280				(248,720)
Charges for services	66,411	66,411	69,856				3,445
Intergovernmental revenues:							
State contributions	4,761,578	5,291,026	5,290,199				(827)
Interest, fines, and penalties	35,000	35,000	59,706			712	712
Other revenues	163,000	163,000	211,652				48,652
Total revenues	8,795,352	9,598,804	9,661,624	527,362	527,362	586,302	58,940
<b>EXPENDITURES</b>							
Current:							
General government	4,450,067	5,236,700	4,889,327				347,373
Public safety	1,022,785	1,008,437	969,121				39,316
Public works	2,342,580	2,884,891	2,829,633				55,258
Recreation	327,790	291,790	262,888				28,902
Health and welfare	652,130	483,899	518,265				(34,366)
Debt service:							
Principal				283,419	283,419	1,800,641	(1,517,222)
Interest				243,943	243,943	311,162	(67,219)
Total expenditures	8,795,352	9,905,717	9,469,234	527,362	527,362	2,111,803	(1,584,441)
<b>OTHER FINANCING SOURCES</b>							
Reprogramming funds	-	306,913	306,913				
Excess of revenues (expenditures) over (under) revenues (expenditures)	\$ -	\$ -	\$ 499,303	\$ -	\$ -	\$ (1,525,501)	\$ (1,525,501)

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**1. ORGANIZATION**

The Municipality of Quebradillas, Puerto Rico (Municipality) was founded in 1823. The Municipality is a political legal entity with full legislative and administrative faculties in every affair of the municipal character, with perpetual succession existence and legal personality, separate and independent from the central government of the Commonwealth of Puerto Rico. The Municipality provides a full range of services including health, public works, environmental control, education, public safety, public housing and community development, culture and recreation as well as many other general and administrative 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 14 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.

The financial information of the Municipality is presented in this report as follows:

- Management's Discussion and Analysis - Introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
- Government - Wide Financial Statements - The 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).

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

- 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 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 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.

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," as amended by GASB Statement No. 39, "Determining whether Certain Organizations are Components Units" – an amendment of GASB Statement No. 14". 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 exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

GASB Statement No. 39 provided additional guidance to determine whether certain organization for which the primary government is not financially accountable should be reported as components units, A legally separate, tax exempt organization should be discretely presented as a component unit if all of the following criteria are met: (a) the economic resources received or held by the separate organization are entirely or almost entirely for the direct benefit of the primary government, its component units, or its constituents; (b) the primary government, or its component units, ins entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the separate organization, and; (c) the economic resources received or held by an individual organization that the specific primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to the primary government. 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 of discrete presentation of the component units' financial data in columns separate from the Municipality's balances and transactions. Based on the aforementioned criteria, the Municipality has no component units.

**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 Municipality. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities are supported mainly by taxes and intergovernmental revenues.

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 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.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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 and the accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus and the modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures 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 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.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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) Debt Service Fund

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

3) SBGP Program

SBGP is used to account for revenues sources for the related activities for the development of viable urban communities by providing decent housing, a suitable living environment, and expanding economic opportunities.

Private-section 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.

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, licenses, permits, 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.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**d. Cash 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 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).

Cash with fiscal agent in the capital projects 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.

**e. Interfund Receivables and Payables**

Activities 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.

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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

	<u>Useful Life</u>
Infrastructure	20-50 years
Buildings and building improvements	20-50 years
Furniture and fixtures	5-20 years
Vehicles and equipment	5-20 years

**g. Reservation of Fund Balance**

Reservations of fund balance represent portions of fund balance 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

Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.

2) Debt Service

Represents net assets available to finance future debt service payments.

3) Capital Project Fund

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.

**h. 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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF QUEBRADILLAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

property tax collections by the Municipal Revenue Collection Center (the "CRIM") for the year ended June 30, 2010 amounted to approximately \$121,560. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$196,107 for workers' compensation insurance covering all municipal employees.

**i. Compensated Absences**

Employees are entitled to 30 days vacations leave and 18 days sick leave per year. Sick leave is recorded as an expenditure in the year paid. Employees are entitled to payment of unused sick leave upon retirement if have been employed for at least 10 years in the municipal government. On July 1997, state Law 152 supra amended the Article 12.016, Section b (2) of the Municipal Law, authorizing the Municipality to pay any excess of vacations and sick leave accumulated over the maximum previously permitted by law. Calculations must be made until December 31 of every year. Excess of sick leave must be paid until March 31 next every natural year. Excess of vacations can be paid after July 1 of every fiscal year.

**j. 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. The most significant estimates consist of the contribution received from the Puerto Rico Electric Power Authority and the Municipal Revenue Collection Center caused by the delay of the notification of the actual revenues and expenditures to the presented in the financial statements of the agencies mentioned above.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**k. Future Adoption of Accounting Pronouncements**

The Governmental Accounting Standards Board (GASB) has issued the following statements that the Municipality has not yet adopted:

<u>Statement Number</u>	<u>Statement Name</u>	<u>Adoption Required in Fiscal Year</u>
54	Fund Balance Reporting and Governmental Fund Type Definitions	2010-11
57	OPEB Measurements by Agent Employers and Agent Multiple – Employer Plans	2011-12
59	Financial Instrument Omnibus	2010-11

The impact of these statements 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 Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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.

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

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

The annual budget is presented in the Combined Statement of Revenues and Expenditures - Budget and Actual (Budgetary Basis) is the budget ordinance to June 30, 2010 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 use for the year ended June 30, 2010 is presented below for the general and debt service funds:

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

	<u>Debt Service</u>
Excess of expenditures over revenues - budgetary basis	\$ (1,525,501)
Entity differences:	
Non-budgeted transfers	1,229,073
Non-budgeted revenue	<u>404,753</u>
Excess of revenues over expenditures - GAAP basis	<u>\$ 108,325</u>

**Explanation of differences:**

**Sources/inflows of resources**

General Fund

Actual amounts (budgetary basis) "available appropriation" from the budgetary comparison schedule	\$ 9,661,624
Differences - budget to GAAP:	
Transfers from other funds are inflows of budgetary resources but are not revenues for financial reporting purposes	(540,293)
Non-budgeted revenues	1,401,368
Reprogrammed funds	<u>306,913</u>
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$ 10,829,612</u>

**Uses/outflows of resources**

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule	\$ 9,469,234
Differences-budget to GAAP:	
Current year encumbrances recorded as expenditures for budgetary purposes	(58,630)
Prior year encumbrances	16,784
Transfers to other funds are outflow of budgetary uses but are not expenditures for financial reporting purposes	(1,769,366)
Non budgeted expenditures	<u>1,968,498</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances	<u>\$ 9,626,520</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**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**

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 payable, are not due and payable in the current period and therefore are not reported in the funds. The details of the approximately \$11.2 million differences are as follows:

Bonds payable	\$ 5,695,000
Compensated absences	1,594,199
Note payable	2,769,600
Accrued interest	451,159
Other long-term liabilities	466,545
Christmas bonus	<u>260,000</u>
Net adjustment to reduce fund balance governmental funds to arrive at net assets of governmental activities	<u><u>\$ 11,236,503</u></u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**5. DEPOSITS**

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. 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 deposits at GDB of approximately \$1,829,987 are restricted principally for capital projects, and the \$1,512,473 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

The Municipality maintains its investments in two (2) banks located at Puerto Rico. All kind of deposit is guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000.

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 QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

The rates are 8.83% for real property and 6.83% 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	2.00%	2.00%
Discounts made by state to tax payer	( .20%)	( .20%)
	<u>8.83%</u>	<u>6.83%</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

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF QUEBRADILLAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year ends. 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.

Currently, the Municipality has received the preliminary settlement from CRIM related to fiscal year 2009-10, but not the final settlement as the six months period after fiscal year ends, 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, 2010, the amount collected by CRIM from taxpayers and charges exceeded the amount advanced by CRIM for the same period by approximately \$97,583. Such amount is presented as due from CRIM in the accompanying financial statements. (See Note 9).

**7. MUNICIPAL LICENSE TAX**

Municipal License Tax receivables are recorded in the fiscal year in which payment is due and, accordingly, represent taxes which are due and uncollected at June 30, 2010. 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 Quebradillas, 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.

**COMMONWEALTH OF PUERTO RICO**  
**MUNICIPALITY OF QUEBRADILLAS**  
**NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)**  
**FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

The rates of municipal license in the Municipality of Quebradillas, are as follows:

Savings and loans associations	= 1.00%
Financial institutions	= 1.50%
Other organizations:	
Up to \$100,000	= .30%
\$100,000 up to \$200,000	= .40%
Over \$200,000	= .50%

The amounts collected in advance are recorded as deferred revenues in the General Fund. The Municipality invoiced and collected in advance during the current year approximately \$442,070, corresponding to the next fiscal year municipal license.

**8. SALES AND USE TAXES**

On July 29, 2007 the Commonwealth Legislature approved Act. No. 80 ("Act. 80") which imposed to all the Municipalities of Puerto Rico a uniform municipal sales and use tax of 1.5%. Effective August 1, 2007 1% of the 1.5% will be collected by the Puerto Rico Department of Treasury.

Act 80 also provides for restrictions on the use of the resources (including the .5 of 1.5% collected by the Commonwealth Government) to be invested in solid waste an recycling programs, capital improvements and health and public safety cost. Amount collected by the Commonwealth Government will be deposited in accounts of special funds in the Government Development Bank of Puerto Rico ("GDB"), subject to restrictions imposed and distributed as follows:

- a. .2% of the .5% will be deposited in a "Municipal Development Fund" to finance costs as restricted by the Act.
- b. .2% of the .5% will be deposited in a "Municipal Redemption Fund" to finance loans to municipalities subject to restrictions imposed by the Act and,
- c. .1% of the .5% will be deposited in a "Municipal Improvement Fund" to finance capital improvement projects; these funds will be distributed based on legislation from the Commonwealth's Legislature.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**9. DUE FROM OTHER AGENCIES**

Represents grants and contributions due from local and federal agencies:

Puerto Rico Electric Power Authority	\$ 1,851,926
CRIM (Preliminary Liquidation 2009-10)	97,583
Labor Department	43,000
OCAM	54,191
U.S. Department of Agriculture	4,037
U.S. Department of Health and Human Services	9,706
	\$ 2,060,443

**10. INTERFUND TRANSACTIONS**

**a. Due From/To Other Funds:**

The due from and due to other fund balances as of June 30, 2010, are as follows:

Receivable Fund	Payable Fund	Amount
General	Other Governmental Funds	\$ 110,294
General	S.B.G.P. Fund	74,454
Other Governmental Funds	General	438,814
		\$ 623,562

The balance of \$438,814 due to the general fund from the Other Governmental Fund represents amount due from prior years related to state contributions' grants.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

Remaining transfers are used to use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

**b. Interfund Transfers:**

Interfund transfers for the year ended June 30, 2010 consisted of the following:

Transfer In	Transfer Out	Amount
Debt Service	General Fund	\$1,769,366
General Fund	Debt Service	<u>540,293</u>
		<u><u>\$2,309,659</u></u>

The transfers are used to (1) move revenues from the fund that statute or budget revenues to collect them to the fund that statute or budget requires to expend them, (2) move receipts restricted to debt service from the fund collection the receipts to the debt service fund as debt service payments become due, and (3) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**11. CAPITAL ASSETS**

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

<u>Primary Government</u>	<u>Balance June 30, 2009</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2010</u>
<b>Governmental Activities:</b>				
Capital assets, not being depreciated:				
Land	\$ 520,000	\$ -	\$ -	\$ 520,000
Construction in progress	983,969	727,034	543,934	1,167,069
Total capital assets, not being depreciated	<u>1,503,969</u>	<u>727,034</u>	<u>543,934</u>	<u>1,687,069</u>
Capital assets, being depreciated:				
Land improvement	1,552,433	-	-	1,552,433
Buildings and building improvements	28,132,311	654,634	-	28,786,945
Equipment	570,801	431,186	-	1,001,987
Vehicles	2,330,570	126,435	-	2,457,005
Infrastructure	3,727,918	149,437	-	3,877,355
Total capital assets, being depreciated	<u>36,314,033</u>	<u>1,361,692</u>	<u>-</u>	<u>37,675,725</u>
Less accumulated depreciation for:				
Land improvement	1,233,199	573,321	-	1,806,520
Buildings and building improvements	2,069,517	53,962	-	2,123,479
Equipment	387,765	78,798	-	466,563
Vehicles	2,078,432	67,630	-	2,146,062
Infrastructure	2,077,092	93,888	-	2,170,980
Total accumulated depreciation	<u>7,846,005</u>	<u>867,599</u>	<u>-</u>	<u>8,713,604</u>
Total capital assets, being depreciated, net	<u>28,468,028</u>	<u>494,093</u>	<u>-</u>	<u>28,962,121</u>
Governmental activities capital assets, net	<u>\$ 29,971,997</u>	<u>\$ 1,221,127</u>	<u>\$ 543,934</u>	<u>\$ 30,649,190</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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

General government	\$ 80,433
Pubic Safety	46,173
Recreation	82,630
Public works	<u>658,363</u>
	<u><u>\$ 867,599</u></u>

**12. DUE TO OTHER AGENCIES**

Due to other agencies at June 30, 2010 is as follows:

Puerto Rico Electric Power Authority	\$ 1,851,926
Department of Housing and Urban Development	3,046
Retirement System Administration	54,042
General Services Administration	37,056
Puerto Rico Water and Sewer Authority	<u>20,964</u>
Total	<u><u>\$ 1,967,034</u></u>

**13. DEFERRED REVENUES**

**a. Municipal License Tax**

The deferred revenues of approximately \$442,070 in the general fund related to municipal license tax collected in fiscal year 2009-10 that will be earned in fiscal year 2010-2011.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**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.

**14. INTERGOVERNMENTAL REVENUES**

Intergovernmental revenues in the general and capital projects funds consist mainly of collections from the Commonwealth of Puerto Rico and the CRIM, and payments in lieu of taxes from the Puerto Rico Electric Power Authority.

**15. LONG-TERM DEBTS**

Bonds and other long-term liabilities outstanding at June 30, 2010 are as follows:

**Bonds**

\$570,000 series of 2002, payable in annual installments of \$10,000 to \$50,000 until July 1, 2026, interest from 2.7% to 5.6%.	\$ 460,000
\$2,000,000 series of 2001, payable in annual installments of \$20,000 to \$175,000 until July 1, 2026, interest from 5% to 7%.	1,670,000
\$638,800 series of 2002, payable in annual installments of \$10,700 to \$49,200 until July 1, 2027, interest from 5% to 7.5%.	529,600
\$670,000 series of 2003, payable in annual installments of \$10,000 to \$50,000 until July 1, 2028, interest from 5% to 7.5%.	570,000
\$2,135,000 series of 2005, payable in annual installments of \$65,000 to \$165,000 until July 1, 2024, interest from 4.37% to 6.5%.	1,695,000

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

\$455,000 series of 2004, payable in annual installments of \$15,000 to \$35,000 until July 1, 2024, interest from 3.27% to 6.5%.	\$ 360,000
\$1,110,000 series of 2008, payable in annual installments of \$25,000 to \$10,000 until July 1, 2027, interest from 6.48% to 7.5%.	1,025,000
\$420,000 series of 2010, payable in annual installments of \$50,000 to \$75,000 until July 1, 2016, interest from 5% to 7%.	375,000
\$1,710,000 series of 2010, payable in annual installments of \$25,000 to \$145,000 until July 1, 2034, interest from 6% to 7.5%.	1,685,000
\$100,000 series of 2010, payable in annual installments of \$5,000 to \$20,000 until July 1, 2026, interest from 6% to 7.5%.	95,000
	95,000
Total bonds and notes payable	\$ 8,464,600

**Other Long-Term Liabilities**

Note payable of \$203,419 represents a repayment agreement with GDB and CRIM to repay the excess of property taxes advances from fiscal years up to 2001. The CRIM will retain principal and interest from the property taxes advances. The amounts retained by CRIM will be remitted to GDB on July 1 of each year through 2032. The repayment agreement is payable in annual aggregate principal installments of \$15,024 plus interest rate of 6.19%.	\$ 178,947
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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

Note payable of \$936,377 represents a financing agreement with the Treasury Department to pay the debt related to social security tax from 1982 to 1986. The financing agreement is payable in monthly installments of \$5,200 plus interest rate of 6%.

\$ 236,657

Note payable of \$268,425 represents a financing agreement with CRIM to the repayment of catastral digitalization. The agreement is due in semester payment of \$18,001 until November 28, 2011, at interest rate of 5.95%.

50,941

Total other long-term liabilities

\$ 466,545

The annual debt service requirements for the bonds payable and note payable at June 30, 2010, are as follows:

	<b>Bonds</b>		<b>Note Payable</b>	
	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>
2011	\$ 230,000	\$ 311,379	\$ 93,000	\$ 139,780
2012	255,000	354,138	99,100	182,054
2013	265,000	352,063	105,400	175,313
2014	285,000	334,566	111,700	168,137
2015	300,000	315,670	123,100	160,526
2016-2020	1,465,000	1,289,456	750,000	665,910
2021-2025	1,650,000	778,820	1,076,900	367,799
2026-2030	725,000	330,575	410,000	40,174
2031-2035	520,000	101,250	-	-
	<u>\$ 5,695,000</u>	<u>\$4,167,917</u>	<u>\$2,769,200</u>	<u>\$ 1,899,693</u>

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

Long-term liability activity for the year ended June 30, 2010 was as follows:

Primary Government	Beginning Balance (As restated)	Additions	Payments	Ending Balance	Due within One Year
<b>Governmental Activities:</b>					
Bonds payable	\$ 3,685,000	\$ 2,230,000	\$ 220,000	\$ 5,695,000	\$ 230,000
Notes payable	2,851,500	-	81,900	2,769,600	93,000
Total long-term debt	<u>6,536,500</u>	<u>2,230,000</u>	<u>301,900</u>	<u>8,464,600</u>	<u>323,000</u>
<b>Other long-term liabilities:</b>					
CRIM - Law 42	182,697		3,750	178,947	3,985
CRIM - LIMS	82,496		31,555	50,941	33,460
Treasury Department	299,057		62,400	236,657	62,400
Employee's Retirement System	1,366,036		1,366,036	-	-
P. R. Water and Sewer Authority	35,000		35,000	-	-
Compensated absences	1,561,111	115,248	82,160	1,594,199	140,500
Total other long-term liabilities	<u>3,526,397</u>	<u>115,248</u>	<u>1,580,901</u>	<u>2,060,744</u>	<u>240,345</u>
Total noncurrent liabilities, governmental activities	<u>\$ 10,062,897</u>	<u>\$ 2,345,248</u>	<u>\$ 1,882,801</u>	<u>\$ 10,525,344</u>	<u>\$ 563,345</u>

## 16. 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 System was created under the ACT 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952.

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 retirement systems.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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 ten (10) years of creditable service, are entitled to an annual benefit, payable monthly for life.

The amounts of the annuity will 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.

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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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, 2010 was approximately \$301,804. The Municipality's payroll for employees covered by ERS was approximately \$3.3 million. The Municipality total payroll for all employees was approximately \$4.5 million.

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

**17. 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

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

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.

**18. LEASES**

**Operating Leases**

Leasing Arrangement with the Municipality as Lessor:

- a. The Municipality leases spaces in its Market Place under operating lease agreements with terms ranging from one to five years.
- b. Total income from leases during the year ended June 30, 2010 was approximately \$26,312.
- c. The Municipality retains title to its leased property. The lessee pays taxes, licenses, insurance, and maintenance costs of the leased assets.

The Municipality is obligated under noncancellable operational leases, with periods not longer than one year.

**19. CONTINGENCIES**

- a. The Municipality receives Federal Grants for specific purposes that are subject to review and audit by the grantor agencies. Although such audits could generate expenditure disallowances under the terms of the grants, management believes that any required reimbursements would not be material.

**20. COMMITMENTS**

The Municipality of Quebradillas had several outstanding or planned construction projects as of June 30, 2010. These projects are evidenced by contractual commitments with contractors. The construction projects are commitments of the Other Governmental Funds that amounted to approximately \$80,137.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**21. RESTATEMENTS**

**a. Net Assets**

Net assets at beginning of year have been adjusted to reflect the following restatements:

Net assets at beginning of year as previously reported	\$22,552,639
Overstatement of long term debts	<u>124,684</u>
Net assets at beginning of year as restated	<u><u>\$22,677,323</u></u>

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

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Disbursements/ Expenditures</u>
<b>U.S. Department of Housing and Urban Development (HUD)</b>		
Direct Programs:		
Section 8 Housing Choice Vouchers	14.871	\$ 187,776
Pass-through Commissioner Office of Municipal Affairs - Community Development Block Grant-States:		
Program SBGP	14.228	687,848
Program SBGP-Recovery Act Funded	14.255	112,868
Pass-through Department of Family: Homelessness Prevention and Rapid Re-Housing Program (Recovery Act Funded)	14.257	29,349
Subtotal U.S. Department of HUD		<u>1,017,841</u>
<b>U.S. Department of Agriculture</b>		
Pass-through Governor's Office of Child Services and Community Development:		
Child and Adult Care Food Program	10.558	40,254
Pass-through Rural Development:		
Rural Housing Preservation Grants	10.433	13,590
Subtotal U.S. Department of Agriculture		<u>53,844</u>
<b>U.S. Department of Justice</b>		
Direct Program:		
Crime Victim Assistance	16.575	58,193
Subtotal U.S. Department of Justice		<u>58,193</u>
<b>U.S. Department of Health and Human Services (HHS)</b>		
Pass-through the Commonwealth of Puerto Rico Governor's Office (Elderly Affairs Office):		
Special Programs for the Aging Title III, Part B, Grants for Supportive Services and Senior Centers	93.044	126,138
Aging Congregate Nutrition Services for States	93.707	6,730
Pass-through the Office of Administration for Children and Families		
Child and Care and Development Block Grant	93.575	203,058
ARRA/Child and Care and Development Block Grant	93.713	13,285
Subtotal U.S. Department of HHS		<u>349,211</u>
<b>U.S. Department of Homeland Security</b>		
State Domestic Preparedness Equipment Support Program	97.004	81,652
Subtotal U.S. Department of Homeland Security		<u>81,652</u>
<b>U.S. Department of Energy</b>		
Pass-through the Puerto Rico Administration of Energy Affairs:		
Energy Efficiency and Conservation Block Grant Program	81.128	20,000
Subtotal U.S. Department of Energy		<u>20,000</u>
<b>TOTAL</b>		<u>\$ 1,580,741</u>

See notes to Schedule of Expenditures of Federal Awards.

ORTIZ, RIVERA & RIVERA & CO.

CERTIFIED PUBLIC ACCOUNTANTS • VALUE ADDED SERVICES

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**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**1. SIGNIFICANT ACCOUNTING POLICIES**

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Quebradillas and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

**2. BASIS OF PRESENTATION**

The expenditures of the schedule are included in the Municipality's basic financial statements in the accompanying Statement of Revenues, Expenditures and Changes in Fund Balances-Governmental Funds. The reconciliation of expenditures in the basic financial statements to the Schedule of Expenditures of Federal Awards is as follows:

	<u>Expenditures</u>
Expenditures as per basic financial statements:	
Federal expenditures included within other governmental funds	\$ 892,893
SBGP Program Fund	<u>687,848</u>
 Total expenditures per schedule of expenditures of federal awards	 <u>\$1,580,741</u>

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

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

We have audited the financial statements of the governmental activities, each major fund and the aggregate remaining fund information of the Municipality of Quebradillas, as of and for the year ended June 30, 2010, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated October 18, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

#### Compliance and Other Matters

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

We noted certain other matters that we reported to management of the Municipality of Quebradillas in a separate letter dated October 18, 2010.

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

San Juan, Puerto Rico  
October 18, 2010

*Ortiz, Rivera, Rivera & Co.*

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to the original of this report.



**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH  
REQUIREMENTS THAT COULD HAVE A DIRECT AND  
MATERIAL EFFECT ON EACH MAJOR PROGRAM AND  
ON INTERNAL CONTROL OVER COMPLIANCE  
IN ACCORDANCE WITH OMB CIRCULAR A-133**

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

Compliance

We have audited Municipality of Quebradillas's compliance with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each Municipality of Quebradillas' major federal programs for the year ended June 30, 2010. Municipality of Quebradillas' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Municipality of Quebradillas' management. Our responsibility is to express and opinion on Municipality of Quebradillas' 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. 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

effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Municipality of Quebradillas' 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 Municipality of Quebradillas compliance with those requirements.

In our opinion, the Municipality of Quebradillas complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2010.

#### Internal Control over Compliance

The management of Municipality of Quebradillas is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Municipality of Quebradillas internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine the 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

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

San Juan, Puerto Rico  
October 18, 2010

*Ortiz, Rivera, Rivera & Co.*

The stamp 2571460 was affixed to the original of this report.



**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**1. SUMMARY OF AUDIT RESULTS**

- a. The auditors' report expresses an unqualified opinion on the basic financial statements of the Municipality of Quebradillas.
- b. There were no significant deficiencies on internal controls over financial reporting.
- c. No instances of noncompliance material to the financial statements of Municipality of Quebradillas were disclosed during the audit.
- d. There were no significant deficiencies on internal controls over major programs.
- e. The auditor's report on compliance with requirements applicable to federal award programs for Municipality of Quebradillas express an unqualified opinion.
- f. Audit findings relative to the major federal award programs for the Municipality of Quebradillas are reported in number 3 of this schedule.
- g. The program tested as major program is:
  - SBGP - CFDA No. 14.228
  - SBGP Recovery Act Funded - CFDA No. 14.255
- h. The threshold for distinguishing types A and B programs was \$300,000.
- i. Municipality of Quebradillas was determined to be a low-risk auditee.

**2. FINDINGS - FINANCIAL STATEMENTS AUDIT**

None

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

During the current examination, follow-up was given to the findings informed to the Municipality in prior years. It was noted that corrective action has been taken, except for certain conditions that still exist and require further action. These are included in the accompanying Schedule of Prior Year Audits Findings and Questioned Costs.

**COMMONWEALTH OF PUERTO RICO  
MUNICIPALITY OF QUEBRADILLAS  
SCHEDULE OF STATUS OF PRIOR YEAR  
AUDIT FINDINGS AND QUESTIONED COSTS (CONTINUED)  
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

<u>Program</u>	<u>Finding/Noncompliance</u>	<u>Status</u>	
<b>SBGP - CFDA No. 14.228</b>	<b>Condition 08-1</b>  The extensions for the year programs contracts were not requested on time.	Condition prevails.	still
<b>SBGP - CFDA No. 14.228</b>	<b>Condition 08-2</b>  The Municipality did not comply with the requirements of filling its financial reports on a timely basis.	Condition corrected.	was
<b>SBGP - CFDA No. 14.228</b>	<b>Condition 09-1</b>  The Federal Program Office does not request the extension of the contracts for the year program 2006 into the 45 days required. The extension for contracts was made on October 22, 2008, which due on August 22, 2008. The Municipality operates approximately two months without a signed contract.	Condition corrected.	was