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

MUNICIPIO DE QUEBRADILLAS
AUDITORÍA 2012-2013

30 DE JUNIO DE 2013

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS

BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED
JUNE 30, 2013

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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PART I – FINANCIAL SECTION

ORR & Co.
Ortiz, Rivera, Rivera & Co.
Certified Public Accountants and Business Advisors

CPA Orlando Luis Ortiz Cabrera
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Members:
American Institute of Certified Public Accountants (AICPA)
AICPA's Private Companies Practice Section (PCPS)
Puerto Rico Board of Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the Municipality of Quebradillas as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor

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considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Municipality of Quebradillas, as of June 30, 2013, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 4 to 10 and 45 to 46 be presented to supplement the basic financial statements. Such information, although not a part of the basic 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, economical, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Quebradillas' basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of

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

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 23, 2013 on our consideration of the Municipality of Quebradillas' internal control over financial reporting an on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant 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 in considering Municipality of Quebradillas' internal control over financial reporting and compliance.

San Juan, Puerto Rico
October 23, 2013

Ortiz, Rivera, Rivera & Co.

The stamp E65041 of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

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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 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's net position of governmental activities increased by $54,608.
- The General Fund (the primary operating fund) reflected, on a current financial resource basis, an increase of $1,827,059.
- On a budgetary basis, actual revenues exceed actual expenditures by $1,197,645.
- Capital expenditures amounted to $581,745.

USING THIS ANNUAL REPORT

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

Government-Wide Financial Statements

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

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

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

Both government-wide financial statements distinguish governmental activities of the Municipality from business-type activities that are intended to recover significant portion of their costs from fees and charges. Governmental activities include general government, public safety, culture and recreation, health and welfare and public work. Business-type activities include park and recreation utilities.

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 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 Position

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. The Municipality's net position of governmental activities totaled $29.4 million at the end of 2013, compared to $30.7 million at the end of the previous year. The business-type activities' net position totaled $2.5 million at the end of 2013, compared to $2.1 of previous year, as restated.

The largest portion of the Municipality's net position 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 position, and these are resources subject to external restrictions for the purposes explained above.

The unrestricted deficit of governmental activities 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.

Municipality of Quebradillas
Condensed Statement of Net Assets
June 30, 2013 and 2012

	Governmental Activities		Business-type Activities		Total	
	2013	2012	2013	2012	2013	2012
Current assets	$ 12,974,029	$ 12,930,775	$ 117,998	$ -	$ 13,092,027	$ 12,930,775
Capital assets	33,525,708	35,857,942	2,412,904	2,016,982	35,938,612	37,874,924
Total assets	46,499,737	48,788,717	2,530,902	2,016,982	49,030,639	50,805,699
Current liabilities	4,018,779	5,587,816	31,917	-	4,050,696	5,587,816
Noncurrent liabilities	13,049,178	12,496,672	-	-	13,049,178	12,496,672
Total liabilities	17,067,957	18,084,488	31,917	-	17,099,874	18,084,488
Invested in capital assets, net of related debt	30,105,244	33,641,358	2,412,904	2,016,982	32,518,148	35,658,340
Restricted	2,826,687	3,702,046	-	-	2,826,687	3,702,046
Unrestricted	(3,500,151)	(6,639,175)	86,081	-	(3,414,070)	(6,639,175)
Total net assets	$ 29,431,780	$ 30,704,229	$ 2,498,985	$ 2,016,982	$ 31,930,765	$ 32,721,211

Changes in Net Position – Governmental Activities

The Municipality's net position increased by $54,608, thirty-two (33%) percent of the Municipality's total revenue came from Taxes generated by the general fund. Federal Grants was eighteen (30%) percent, while the State Contributions made forty (34%) percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for general government, public works and public safety.

Changes in Net Position – Business-type Activities

The Municipality's net position increased by $482,003; ninety two (92%) percent of total revenues came from contributions generated by general fund, and the eight (8%) percent came from charges of services.

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 $9,230,250 an increase of $371,441 in comparison with the prior year. There are reservations of fund balance amounting to $6,315,716.

The general fund is included within the governmental funds; it is the chief operating fund of the Municipality. As of June 30, 2013, the general fund has a balance of $4,154,469. The prior year surplus of $2,327,410 was increased by $1,827,059 during fiscal year 2013.

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 decreased by $839,246 compared with the prior year. The increase in fund balance is directly related to a transfer-in from Debt Services Fund. The actual revenues diminished the revised budget revenues by $121,796 (net). The most significant variance was the state contribution with $656,695.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2013, amounts to $45.4 million, net of accumulated depreciation of $11.9 million, leaving a net book value of $33.5 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 $626,080 of capital assets during the fiscal year 2012-2013. Capital assets acquired during the year were as follows:

- Construction in Progress - $50,983
- Building and building improvements - $408,610
- Infrastructure - $79,257
- Acquisition of Equipment and Vehicles - $87,230

Other projects related to repair and maintenance of roads (not capitalized) was development during the year 2013.

Debt Administration

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

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

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal 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 CPA Mariannet Padín Cubero, Chief Financial Officer on the Finance Offices in the Central Town, Quebradillas, Puerto Rico.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
STATEMENT OF NET POSITION
JUNE 30, 2013

	Primary Government		
	Governmental Activities	Business-Type Activities	Total Primary Government
Assets			
Cash in bank **(Notes 2 and 4)**	$ 4,185,007	$ 117,998	$ 4,303,005
Cash with fiscal agent **(Notes 2 and 4)**	5,513,880		5,513,880
Accounts receivable:			
Property taxes	8,759		8,759
Sales and use taxes	86,419		86,419
Proprietary fund	31,917		31,917
Due from other agencies **(Note 8)**	3,148,047		3,148,047
Capital assets, net **(Note 10)**	33,525,708	2,412,904	35,938,612
Total assets	$ 46,499,737	$ 2,530,902	$ 49,030,639
Liabilities and Net Position			
Liabilities			
Accounts payable and accrued liabilities	$ 794,517	$ 31,917	$ 826,434
Due to other agencies **(Note 11)**	2,142,800		2,142,800
Matured bonds and interest payable	518,479		518,479
Deferred revenues **(Note 12)**:			
Municipal license tax	548,983		548,983
Claims and judgments	14,000		14,000
Noncurrent liabilities **(Note 14)**:			
Due within one year	510,241		510,241
Due in more than one year	11,992,873		11,992,873
Accrued interest	546,064		546,064
Total liabilities	17,067,957	31,917	17,099,874
Net Position			
Investment in capital assets, net of related debt	30,105,244	2,412,904	32,518,148
Restricted for:			
Debt service	1,302,151		1,302,151
Capital projects	1,524,536		1,524,536
Unrestricted	(3,500,151)	86,081	(3,414,070)
Total net position	29,431,780	2,498,985	31,930,765
Total liabilities and net position	$ 46,499,737	$ 2,530,902	$ 49,030,639

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, 2013

		Program Revenues			Net (Expense) Revenues and Changes in Net Position	
					Primary Government	
Functions/Programs	**Expenses**	**Charges for Services**	**Operating Grants and Contributions**	**Capital Grants and Contributions**	**Governmental Activities**	**Business-Type Activities**
Governmental activities:						
General government	$ 5,686,085	$ 489,639	$ -	$ -	$ (5,196,446)	$ -
Public safety	1,693,835				(1,693,835)	
Culture and recreation	522,380		514,137		(8,243)	
Health and welfare	3,132,491		2,283,792		(848,699)	
Public work	4,780,941			2,050,056	(2,730,885)	
Interest on long-term debt	377,444				(377,444)	
Total governmental activities	16,193,176	489,639	2,797,929	2,050,056	(10,855,552)	-
Business-Type Activities:						
Aquatic Park	159,547	198,018	-	443,532	-	482,003
Total primary government	$ 16,352,723	$ 687,657	$ 2,797,929	$ 2,493,588	$ (10,855,552)	$ 482,003
General revenues:						
Property taxes **(Note 5)**					2,446,271	-
Municipal license tax **(Note 6)**					927,064	-
Sales and use taxes **(Note 7)**					1,497,890	-
Grants and contributions not restricted to specific programs					5,556,985	-
Interest, fines and penalties					294,348	-
Miscellaneous					187,602	-
Total general revenues					10,910,160	-
Change in net position					54,608	482,003
Net position at beginning of year, as restated **(Note 22)**					29,377,172	2,016,982
Net position at end of year					$ 29,431,780	$ 2,498,985

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, 2013

Assets	General	Debt Service	Head Start Program	Loan $3,635,000	Other Governmental Funds	Total Governmental Funds
Cash in bank **(Notes 2 and 4)**	$3,380,549	$ -	$ 49,641	$ -	$ 754,817	$ 4,185,007
Cash with fiscal agent **(Notes 2 and 4)**		2,922,762		1,524,536	1,066,582	5,513,880
Accounts receivable:						
Property taxes		8,759				8,759
Sales and use taxes	43,729	42,690				86,419
Proprietary fund	31,917					31,917
Due from other agencies **(Note 8)**	2,087,399		889,159		171,489	3,148,047
Due from other funds **(Note 9)**	1,806,685				195,125	2,001,810
Total assets	$7,350,279	$2,974,211	$ 938,800	$1,524,536	$ 2,188,013	$ 14,975,839

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
BALANCE SHEET-GOVERNMENTAL FUNDS (CONTINUED)
JUNE 30, 2013

Liabilities and Fund Balances	General	Debt Service	Head Start Program	Loan $3,635,000	Other Governmental Funds	Total Governmental Funds
Liabilities						
Accounts payable and accrued liabilities	$ 294,902	$ -	$ 70,629	$ -	$ 153,986	$ 519,517
Due to other funds **(Note 9)**	195,125	1,153,581	506,355		146,749	2,001,810
Due to other agencies **(Note 11)**	2,142,800					2,142,800
General obligations: **(Note 14)**						
Bonds		320,000				320,000
Interest		198,479				198,479
Deferred revenues: **(Note 12)**						
Municipal license tax	548,983					548,983
Claims and judgments	14,000					14,000
Total liabilities	3,195,810	1,672,060	576,984	-	300,735	5,745,589
Fund Balances						
Restricted		1,302,151	361,816		900,700	2,564,667
Committed				1,524,536	979,347	2,503,883
Assigned	1,244,310				2,856	1,247,166
Unassigned	2,910,159				4,375	2,914,534
Total fund balances	4,154,469	1,302,151	361,816	1,524,536	1,887,278	9,230,250
Total liabilities and fund balances	$7,350,279	$2,974,211	$ 938,800	$1,524,536	$ 2,188,013	$ 14,975,839

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO THE STATEMENT OF NET POSITION
JUNE 30, 2013

Total fund balances - governmental funds	$ 9,230,250
Amounts reported for governmental activities in the statement of net position 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.	33,525,708
• Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the governmental funds. **(Note 3)**	(13,324,178)
Net position of governmental activities	$ 29,431,780

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

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, 2013

	General	Debt Service	Head Start Program	Loan $3,635,000	Other Governmental Funds	Total Governmental Funds
REVENUES						
Property taxes **(Note 5)**	$ 1,949,194	$ 497,077	$ -	$ -	$ -	$ 2,446,271
Municipal license taxes **(Note 6)**	927,064					927,064
Sales and use taxes **(Note 7)**	999,452	498,438				1,497,890
Licenses, permits, and other local taxes	459,055					459,055
Charges for services	30,584					30,584
Intergovernmental revenues **(Note 13)**:						
Federal grants and contributions			2,283,792		2,564,193	4,847,985
State contributions	5,273,102				283,883	5,556,985
Interest, fines, and penalties	291,913	2,435				294,348
Other revenues	163,353				24,249	187,602
Total revenues	10,093,717	997,950	2,283,792	-	2,872,325	16,247,784
EXPENDITURES						
Current:						
General government	5,118,560				147,028	5,265,588
Public safety	1,489,657				124,165	1,613,822
Health and welfare	624,063		1,921,976		586,452	3,132,491
Culture and recreation	225,918				195,142	421,060
Public works	1,744,273				2,179,868	3,924,141
Capital outlays					581,745	581,745
Debt service:						
Principal		492,302				492,302
Interest and other		445,194				445,194
Total expenditures	9,202,471	937,496	1,921,976	-	3,814,400	15,876,343
Excess (deficiency) of revenues over (under) expenditures	891,246	60,454	361,816	-	(942,075)	371,441
OTHER FINANCING SOURCES (USES)						
Transfers in	1,154,750	218,937				1,373,687
Transfers out	(218,937)	(1,154,750)			-	(1,373,687)
Total other financing sources	935,813	(935,813)	-	-	-	-
Net change in total fund balances	1,827,059	(875,359)	361,816		(942,075)	371,441
FUND BALANCES AT BEGINNING OF YEAR	2,327,410	2,177,510		1,524,536	2,829,353	8,858,809
FUND BALANCES AT END OF YEAR	$ 4,154,469	$ 1,302,151	$ 361,816	$ 1,524,536	$ 1,887,278	$ 9,230,250

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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, 2013

Net change in fund balances - total governmental funds	$ 371,441
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.	581,745
• 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.	(1,143,390)
• 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.	492,302
• Change in accrued interest expense which does not require the use of current financial resources.	67,750
• 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.	(315,240)
Changes in net position of governmental activities	$ 54,608

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
STATEMENT OF NET POSITION
PROPRIETARY FUND
JUNE 30, 2013

	Aquatic Park Fund
Assets	
Cash in bank	$ 117,998
Capital assets, net **(Note 10)**	2,412,904
Total assets	$ 2,530,902
Liabilities and Net Position	
Liabilities	
Accounts payable and accrued liabilities	$ 31,917
Total liabilities	31,917
Net Position	
Net investment in capital assets	2,412,904
Unrestricted	86,081
Total net position	2,498,985
Total liabilities and net position	$ 2,530,902

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
PROPRIETARY FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	Aquatic Park Fund
OPERATING INCOME:	
Charges for services	$ 198,018
Total operating revenues	198,018
OPERATING EXPENSES:	
Salaries	59,175
Fringe benefits	6,777
Insurance	10,240
Office materials	1,740
Equipment	3,972
Maintenance materials	21,624
Miscellaneous	7,551
Bank charges	858
Depreciation **(Note 10)**	47,610
Total operating expenses	159,547
Operating income	38,471
CAPITAL CONTRIBUTION	443,532
CHANGE IN NET POSITION	482,003
TOTAL NET POSITION, BEGINNING, AS RESTATED (Note 22)	2,016,982
TOTAL NET POSITION, ENDING	$ 2,498,985

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	Aquatic Park Fund
CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from customers	$ 198,018
Payments to employees of services	(59,175)
Payment for insurance	(10,240)
Payments to suppliers	(10,605)
Net cash provided by operating activities:	117,998
NET INCREASE IN CASH	117,998
CASH AT BEGINNING OF YEAR	-
CASH AT ENDING OF YEAR	$ 117,998
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES	
Operating income	$ 38,471
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	47,610
Increase in accounts payable	31,917
Total adjustments	79,527
Net cash provided by operating activities	$ 117,998

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, 2013

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 and 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).

- Statement of Net Position - The statement of net position is designed to display the financial position of the Municipality, including capital assets and infrastructure.

The net position 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

A reporting entity is comprised of the primary government, component units and other organizations that are included to ensure that financial statements are not misleading. The primary government consists of all funds, departments, boards and agencies that are not legally separate from the Municipality and for which the Municipality is financial accountable.

The Municipality's management has considered all potential component units (whether governmental, not-for-profit, or profit-oriented) for which it may be financially accountable, and other legally separate organizations for which the Municipality is not financially accountable but the nature and significance of their relationship with the Municipality may be such that exclusion of their basic financial statements from those of the Municipality would cause the accompanying basic financial statements to be misleading or incomplete. Accordingly, a legally separate organization would be reported as a component unity of the Municipality if all of the following criteria are met:

1) The Mayor appoints a voting majority of an organization's governing body and, either (1) the Municipality has the ability to impose its will on that organization

or (2) the organization has the potential to provide specific financial benefits to, or impose specific financial burdens on the Municipality.

2) The economic resources, for which the Municipality is entitled, either received or held by the separate organization, are entirely or almost entirely for the direct benefit of the Municipality or its constituents.

GAAP details two methods of presentation: blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component units' financial data in columns separate from the Municipality's balances and transactions.

The Municipality's management has concluded that, based on the aforementioned criteria, there are no legally separate entities or organizations that should be reported as component units of the Municipality for the fiscal year ended June 30, 2013.

b. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of changes in net position) report information on all the activities of the Municipality.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segments 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.

The effect of all inter-fund activities (assets, liabilities, revenues, expenditures and other financing sources/uses among governmental funds) have been eliminated from the governmental-wide financial statements.

Separate fund financial statements are provided for governmental funds and proprietary funds. Major governmental funds are reported on separate columns to 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.

On July 1, 2012, the Municipality adopted the provision of GASB 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.* GASB 63 provides guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position and related disclosures. The statement of net assets is renamed the statement of net position and includes four components: assets, deferred outflows of resources, liabilities and deferred inflows of resources.

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

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as *current financial resources* or *economic resources.* The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

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

The governmental fund financial statements are reported using the *current financial resources measurements focus* and the *modified accrual basis of accounting.* Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current

period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, and claims and judgments, are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Issuance of long-term debt and acquisitions under capital leases are reported as other financing sources.

Property taxes, sales 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. Entitlements are recorded as revenues when all eligibility requirements are met, including any time requirements, and the amount is received during the period or within the availability period for this revenue source (within 60 days or year-end). Expenditures-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the government.

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.

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) Head Start Program

This fund account for revenue sources to provide essential human services such as improving maternal and infant health, pre-school education and services, prevent child abuse and domestic violence and medical and social science research including the prevention of the outbreak of infectious disease and immunization services.

4) Loan $3,635,000

The Loan $3,635,000 fund is used to account for the financial resources for the acquisition of personal property and/or construction of major improvements which are not financed by other funds.

The government reports the following major proprietary fund:

The Aquatic Park accounts for the operation, maintenance, administration of aquatic park facilities. Operating revenues and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenues are charges to customers for sales and services. Operating expenses includes the cost of sales and services, administrative expenses, and depreciation on capital assets.

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). The Municipality's policy is to invest any excess cash in certificates of deposits with institutions qualified by the PRTD. Earnings from these funds are recorded in the corresponding fund.

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.

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

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

g. Fund Balances

The Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB No. 54), which enhanced the usefulness of fund balance information by providing clearer

fund balance classifications that can be more consistently applied. This statement establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which the Municipality is bound to observe constraints imposed upon the use of the resources reported in governmental funds.

Pursuant to the provisions of GASB No. 54, the accompanying fund financial statements report fund balance amounts that are considered nonspendable, such as fund balance associated with inventories. Other fund balances have been reported as restricted, committed, assigned, and unassigned, based on the relative strength of the constraints that control how specific amounts can be spent, as described as follows:

1) *Nonspendable* - Represent resources that cannot be spent readily with cash or are legally or contractually required not be spent, including but not limited to inventories, prepaid items, and long term balances of interfund loans and accounts receivable.

2) *Restricted* - Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditors or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.

3) *Committed* - Represent resources used for specific purposes, imposed by formal action of the Municipal's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.

4) *Assigned* - Represent resources intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed (generally executive orders approved by the Mayor). Intent can be expressed by the Municipal Legislature, the Mayor or by an official or body to which the Municipal Legislature delegates authority in conformity with the Autonomous Municipalities Act of Puerto Rico, as amended. In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.

5) *Unassigned* - Represent the residual classification for the Municipality's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

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

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balance amounts as of and for the fiscal year ended June 30, 2013.

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

The classification of the Municipality's individual governmental funds among general, debt service, special revenue, and capital projects fund types used in prior fiscal years for financial reporting purposes was not affected by the implementation of GASB No. 54.

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 property tax collections by the Municipal Revenue Collection Center (the "CRIM")

for the year ended June 30, 2013 amounted to $359,185. The current insurance policies have not been cancelled or terminated. The CRIM also deducted $145,723 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 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.

k. Future Adoption of Accounting Pronouncements

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

Statement Number	Statement Name	Adoption Required in Fiscal Year
65	Items Previously Reported as Assets and Liabilities	2013-14
66	Technical Corrections - 2012- an amendment of GASB Statements No. 10 and 62	2013-14
67	Financial Reporting for Pension Plans - an amendment of GASB Statement No. 25	2013-14
68	Accounting and Financial Reporting for Pensions - and amendment of GASB Statement No. 27	2014-15
69	Government Combinations and Disposals of Government Operations	2013-14
70	Accounting for Financial Reporting for Non-exchange Financial Guarantees	2013-14

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

l. Deferred Inflows

On July 1, 2012 the Municipality adopted the provisions of GASB Statement No. 63, *Financial Reporting of deferred Outflows of resources, Deferred Inflows of Resources, and Net Position* (GASB No. 63).

In the GFFS, deferred inflows arises when one of the following situations occur:

- Potential revenue does not meet both the "measurable" and "available" criteria for revenue recognition in the current period (reported as *"earned but unavailable revenue"* in the accompanying balance sheet-governmental funds). As previously discussed, available is defined as due (or past due) at June 30, 2013 and collected within 90 days (60 days for property taxes) thereafter to pay obligations due at June 30. In subsequent periods, when both criteria (measurable and available) are met, the liability for deferred revenue is removed and revenue is recognized.

- The Municipality receives resources before it has a legal claim to them (reported as *"unearned revenue"* in the accompanying balance sheet-governmental funds). In subsequent periods, when the revenue recognition criterion is met, the liability for deferred inflows is removed and revenue is recognized.

Deferred inflows at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them (reported as *"unearned revenue"* in the accompanying statement of net position). No *"earned but unavailable revenue"* is accounted for in the accompanying statement of net position.

3. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

The governmental fund balance sheet includes reconciliation between fund balance-governmental funds and net position of governmental activities as reported in the government-wide statement of net position. 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 $13.3 million difference is as follows:

Bonds payable	$ 4,945,000
Compensated absences	1,345,333
Notes payable	5,997,100
Accrued interest	546,064
Other long-term liabilities	215,681
Christmas bonus	275,000
Net adjustment to reduce fund balance governmental funds to arrive at net position of governmental activities	$13,324,178

4. 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 $2,629,582 are restricted principally for capital projects, and the $2,922,762 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 one bank 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.

5. 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.

The rates are 8.83% for real property and 6.83% for personal property. The composition is as follows:

	Real	Personal
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%)
	8.83%	6.83%

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 ensuring fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year 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 2012-13, 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, 2013, the amount collected by CRIM from taxpayers and charges exceeded the amount advanced by CRIM for the same period by approximately $42,783. Such amount is presented as due from CRIM in the accompanying financial statements. (See note 8).

6. 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, 2013. The annual Municipal License Tax is determined based on the gross income of all commerce and industrial organizations that 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.

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 $548,983, corresponding to the next fiscal year municipal license.

7. 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 and 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.

8. DUE FROM OTHER AGENCIES

Represents grants and contributions due from local and federal agencies:

Puerto Rico Electric Power Authority	$ 2,044,616
Administration for Children and Family (Head Start)	889,159
OCAM	98,634
CRIM (Preliminary Liquidation 2012-13)	42,783
Labor Department	41,760
Administration for Children and Family (Food Program)	31,095
	$ 3,148,047

9. INTERFUND TRANSACTIONS

a. Due From/To Other Funds:

The due from and due to other fund balances as of June 30, 2013, are as follows:

Receivable Fund	Payable Fund	Amount
General	Debt Service	$ 1,153,581
General	Head Start Program	506,355
General	Other Governmental Funds	146,749
Other Governmental	General	195,125
		$ 2,001,810

The balance of $195,125 due to the general fund from the Other Governmental Fund represents amount due from prior years related to state contributions' grants. 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, 2013 consisted of the following:

Transfer In	Transfer Out	Amount
General Fund	Debt Service	$ 1,154,750
Debt Service	General Fund	218,937
		$ 1,373,687

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, (3) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

10. CAPITAL ASSETS

a. Primary Government

Capital asset activity for the Municipality for the year ended June 30, 2013 was as follows:

Primary Government	Balance June 30, 2012 as restated	Increases	Decreases	Balance June 30, 2013
Governmental Activities:				
Capital assets, not being depreciated:				
Land	$ 1,169,925	$ -	$ -	$ 1,169,925
Construction in progress	636,156	50,983	487,867	199,272
Total capital assets, not being depreciated	1,806,081	50,983	487,867	1,369,197
Capital assets, being depreciated:				
Land improvement	1,552,433		-	1,552,433
Buildings and building improvements	33,174,656	408,610	-	33,583,266
Equipment	1,054,953	72,230	-	1,127,183
Work of Arts	22,000		-	22,000
Vehicles	2,677,483	15,000	-	2,692,483
Infrastructure	5,016,641	79,257	-	5,095,898
Total capital assets, being depreciated	43,498,166	575,097	-	44,073,263
Less accumulated depreciation for:				
Land improvement	2,598,305	698,959	-	3,297,264
Buildings and building improvements	2,703,116	53,632	-	2,756,748
Equipment	729,669	154,112	-	883,781
Work of Arts	2,750	2,750	-	5,500
Vehicles	2,314,907	94,190	-	2,409,097
Infrastructure	2,424,615	139,747	-	2,564,362
Total accumulated depreciation	10,773,362	1,143,390	-	11,916,752
Total capital assets, being depreciated, net	32,724,804	(568,293)	-	32,156,511
Governmental activities capital assets, net	$ 34,530,885	$ (517,310)	$ 487,867	$ 33,525,708

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

General government	$ 105,257
Public safety	80,013
Recreation	101,320
Public works	856,800
Total depreciation expense-governmental activities	$ 1,143,390

b. Business-Type Government

Business-type government	Balance June 30, 2012 as restated	Increases	Decreases	Balance June 30, 2013
Governmental Activities:				
Capital assets, not being depreciated:				
Land	$ 40,000	$ -	$ -	$ 40,000
Total capital assets, not being depreciated	40,000	-	-	40,000
Capital assets, being depreciated:				
Building	1,976,982	443,532	-	2,420,514
Total capital assets, being depreciated	1,976,982	443,532	-	2,420,514
Less accumulated depreciation for:				
Building	-	47,610	-	47,610
Total accumulated depreciation	-	47,610	-	47,610
Total capital assets, being depreciated, net	1,976,982	395,922	-	2,372,904
Business type government assets	$ 2,016,982	$ 395,922	$ -	$ 2,412,904

11. DUE TO OTHER AGENCIES

Puerto Rico Electric Power Authority	$2,044,615
Retirement System Administration	49,151
General Services Administration	34,530
Puerto Rico Water and Sewer Authority	14,504
Total	$2,142,800

12. DEFERRED REVENUES

a. Municipal License Tax

The deferred revenues of approximately $548,983 in the general fund related to municipal license tax collected in fiscal year 2012-2013 that will be earned in fiscal year 2013-2014.

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.

13. 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.

14. LONG-TERM DEBTS

Bonds and other long-term liabilities outstanding at June 30, 2013, are as follows:

$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%.	$ 405,000
$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%.	1,490,000
$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%.	472,100
$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%.	510,000

$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%.	$ 1,425,000
$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%.	300,000
$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%.	925,000
$420,000 series of 2010, payable in annual installments of $50,000 to $75,000 until July 1, 2016, interest from 5% to 7%.	210,000
$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%.	1,600,000
$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%.	80,000
$3,635,000 series of 2012, payable in annual installments of $55,000 to $310,000 until July 1, 2036, interest from 6% to 7.5%.	3,525,000
Total bonds and notes payable	$ 10,942,100

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 the 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%.	$ 166,224
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%.	49,457
Total other long-term liabilities	$ 215,681

The annual debt service requirements for the bonds payable and notes payable at June 30, 2013, are as follows:

	Bonds		*Notes Payable*	
	Principal	Interest	Principal	Interest
2014	$ 285,000	$ 242,944	$ 171,700	$ 303,120
2015	300,000	293,570	188,100	384,174
2016	325,000	275,410	199,600	372,238
2017	260,000	255,732	211,200	359,562
2018	275,000	239,930	237,900	346,165
2019-2023	1,650,000	949,358	1,454,100	1,537,984
2024-2028	1,120,000	462,670	1,619,500	1,031,413
2029-2033	585,000	192,000	1,060,000	570,375
2034-2038	145,000	10,875	855,000	132,000
	$ 4,945,000	$2,922,489	$ 5,997,100	$ 5,037,031

Long-term liability activity for the year ended June 30, 2013, was as follows:

Primary Government	Beginning Balance	Additions	Payments	Ending Balance	Due within One Year
Governmental Activities:					
Bonds payable	$ 5,210,000	$ -	$ 265,000	$ 4,945,000	$ 285,000
Notes payable	6,157,500	-	160,400	5,997,100	171,000
Total long-term debt	11,367,500	-	425,400	10,942,100	456,000
Other long-term liabilities:					
CRIM - Law 42	170,726		4,502	166,224	4,784
Treasury Department	111,857		62,400	49,457	49,457
Compensated absences	1,488,625		143,292	1,345,333	-
Total other long-term liabilities	1,771,208	-	210,194	1,561,014	54,241
Total noncurrent liabilities, governmental activities	$ 13,138,708	$ -	$ 635,594	$ 12,503,114	$ 510,241

15. FUND BALANCES

	General	Debt Service	Head Start Program	Loan $3,650,000	Other Governmental Funds	Total
Restricted:						
General government	$ -	$ -	$ -	$ -	$ 30,552	$ 30,552
Public safety					712	712
Public works					832,840	832,840
Health and welfare					30,964	30,964
Education					5,632	5,632
Debt service		1,302,151				1,302,151
Committed:						
Public works				1,524,536	979,347	2,503,883
Education			361,816			361,816
Assigned:						
General government	1,229,833					1,229,833
Public safety	248					248
Culture and recreation	2,084					2,084
Health and welfare	12,145				2,856	15,001
Unassigned	2,852,940				4,375	2,857,315
	$4,097,250	$1,302,151	$ 361,816	$1,524,536	$ 1,887,278	$ 9,173,031

16. NET POSITION

Net position invested in capital assets, net of related debt, is comprised of the following:

Capital assets, net of accumulated	$ 33,525,708
Outstanding balance on capital related debt	(4,945,000)
Unspent capital debt proceeds	1,524,536
Total invested in capital assets, net of related	$ 30,105,244

17. 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.

Participation is mandatory except for members of the Legislature, Government Secretaries, Agency Heads 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 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 (10.275% 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 11.275% of gross salary. Contributions' requirements are established by law. The actuarially determined contribution requirement and contributions actually made for the year ended June 30, 2013 was approximately $246,731. The Municipality's payroll for employees covered by ERS was approximately $2.2 million. The Municipality total payroll for all employees was approximately $5.6 million.

Additional information on the ERS is provided in its financial statements for the year ended June 30, 2013, a copy of which can be obtained from the ERS, Minillas Station, PO Box 42003, San Juan, PR 00940.

18. RISK MANAGEMENT

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

19. 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, 2013 was approximately $25,824.

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.

20. CONTINGENCIES

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.

21. COMMITMENTS

The Municipality of Quebradillas had outstanding or planned construction projects as of June 30, 2013. These projects are evidenced by contractual commitments with contractors. The construction projects are commitments of the Other Governmental Funds that amounted to approximately $16,812.

22. RESTATEMENTS

The beginning net position of the statement of net position for the Governmental and Business Type Activities has been restated to reclassify amount of capital assets and to adding additional assets as follows:

	Governmental Activities	Business-Type Activities
Beginning net assets, as previously recorded	$ 30,704,229	$ -
Reclassification of net assets	(1,976,982)	1,976,982
Understatement of capital assets	649,925	40,000
Beginning net assets, as restated	$ 29,377,172	$ 2,016,982

23. SUBSEQUENT EVENTS

In preparing these financial statements, the Municipality has evaluated events and transactions for potential recognition or disclosure through October 23, 2013, the date the financial statements were available to be issued.

PART II – REQUIRED SUPPLEMENTARY INFORMATION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget- Positive (Negative)
	Original	Final		
REVENUES				
Property taxes	$ 509,182	$ 509,182	$ 509,182	$ -
Municipal license taxes	564,000	656,145	938,870	282,725
Sales and use taxes	820,000	839,892	998,894	159,002
Licenses and permits	268,500	352,668	379,316	26,648
Charges for services and rent	34,000	26,975	29,670	2,695
Intergovernmental revenues:				
State contributions	7,306,002	7,318,783	6,662,088	(656,695)
Interest, fines and penalties	115,000	235,248	288,898	53,650
Other revenues	121,389	99,980	110,159	10,179
Total revenues	9,738,073	10,038,873	9,917,077	(121,796)
EXPENDITURES				
Current:				
General government	4,575,448	5,521,802	5,000,326	521,476
Public safety	929,718	726,132	695,577	30,555
Public works	3,153,221	3,254,541	2,548,836	705,705
Recreation	313,705	257,275	230,280	26,995
Health and welfare	765,981	681,428	646,718	34,710
Total expenditures	9,738,073	10,441,178	9,121,737	1,319,441
OTHER FINANCING SOURCES				
Reprogramming funds	-	402,305	402,305	-
Excess of revenues over expenditures	$ -	$ -	$ 1,197,645	$ 1,197,645

Explanation of Differences:

Sources/Inflows of resources:	
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule	$ 9,917,077
Differences - budget to GAAP:	
Net change in receivables	176,640
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances	$ 10,093,717
Uses/outflows of resources:	
Actual amounts (budgetary basis) "total changes to appropriations" from the budgetary comparison schedule	$ 9,121,737
Differences - budget to GAAP:	
Prior year encumbrances recorded as current year expenditures for GAAP basis	(54,047)
Net change in payables	(110,582)
Current year encumbrances recorded as expenditures for budgetary purposes	245,363
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances	$ 9,202,471

The accompanying note to Budgetary Comparison Schedule is an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
NOTE TO BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

NOTE 1 - STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Budgetary Control

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with accounting principles generally accepted in the United States of America, 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 certain appropriations within the budget known as Mayor's Executive Orders do not require the approval of the Municipal Legislature. The Municipality prepares its annual budget including the operations of the general fund.

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

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

The annual budget as presented in the Budgetary Comparison Schedule – General Fund is the budget resolutions at June 30, 2013 representing the original budget.

PART III – SINGLE AUDIT

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

Federal Grantor/Program Title	Federal CFDA Number	Federal Disbursements/ Expenditures
U.S. Department of Housing and Urban Development (HUD)		
Direct Programs:		
Section 8 Housing Choice Vouchers	14.871	$ 246,423
Pass-through Commissioner Office of Municipal Affairs -		
Community Development Block Grant/State's Program	14.228	897,805
Neighborhood Stabilization Program (NSP1) - Recovery Act Funded	14.228	203,957
Neighborhood Stabilization Program (NSP3) - Recovery Act Funded	14.228	479,950
Pass-through Department of Family:		
Emergency Shelter Grants Program (Prevention)	14.231	10,834
Homelessness Prevention and Rapid Re-Housing Program (Recovery Act Funded)	14.257	61,331
Subtotal U.S. Department of HUD		1,900,300
U.S. Department of Agriculture		
Pass-through Education Department:		
Child and Adult Care Food Program-Child Care	10.558	28,265
Child and Adult Care Food Program-Head Start	10.558	167,348
Subtotal U.S. Department of Agriculture		195,613
U.S. Department of Justice		
Direct Program:		
Crime Victim Assistance	16.575	49,768
Subtotal U.S. Department of Justice		49,768
U.S. Department of Health and Human Services (HHS)		
Pass-through the Puerto Rico Governor's Office (Elderly Affairs Office):		
Special Programs for the Aging, Title III, Part C	93.045	24,804
Special Programs for the Aging, Title III, Part D	93.043	7,055
Nutrition Services Incentive Program	93.053	27,211
Pass-through the Office of Administration for Children and Families:		
Child and Care and Development Block Grant	93.575	203,474
Pass-through the Office of Administration for Children and Families:		
Head Start	93.600	1,921,976
Subtotal U.S. Department of HHS		2,184,520
U.S. Department of Energy		
Pass-through the Puerto Rico Administration of Energy Affairs:		
Energy Efficiency and Conservation Block Grant Program	81.128	86,919
Subtotal U.S. Department of Energy		86,919
TOTAL		$ 4,417,120

See notes to schedule of Expenditures of Federal Awards.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

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 a follows:

	Expenditures
Expenditures as per basic financial statements:	
Federal expenditures included within:	
Other governmental funds	$ 2,495,144
Head start program	1,921,976
Total	$ 4,417,120
Total expenditures per schedule of expenditures of federal awards	$ 4,417,120

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Puerto Rico Board of Certified Public Accountants

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, in accordance with the 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, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Municipality of Quebradillas', as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements, and have issued our report thereon date October 23, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Municipality's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but no for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control. Accordingly, we do not express an opinion on the effectiveness of the Municipality's internal control.

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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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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 that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Purpose of this Report

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

San Juan, Puerto Rico
October 23, 2013

Ortiz, Rivera, Rivera & Co.

The stamp E 65042 of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

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

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

Report on Compliance for each Major Federal Program

We have audited Municipality of Quebradillas' compliance with the types of compliance requirements described in the *OMB Circular A-133* Compliance Supplement that could have a direct and material effect on each of Municipality's major federal programs for the year ended June 30, 2013. Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditors' Responsibility

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

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

Opinion on Each Major Federal Program

In our opinion, the Municipality complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2013.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2013-1 to 2013-3. Our opinion on each major federal program is not modified with respect to these matters.

Municipality's response to the noncompliance findings identified in our audit is described in the accompanying corrective action plan. Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control over Compliance

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

program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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 material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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

Ortiz, Rivera, Rivera & Co.

San Juan, Puerto Rico
October 23, 2013

The stamp E65043 of the Puerto Rico Society of Certified Public Accountants was affixed to the original of this report.

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF QUEBRADILLAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2013

1. SUMMARY OF AUDIT RESULTS

Financial Statements

Type of auditor's report issued:	Unqualified opinion	
Internal control over financial reporting:		
Material weakness (es) identified?	___ Yes	X No
Significant deficiency (ies) identified?	___ Yes	X No
Noncompliance material to financial statements noted?	___ Yes	X No

Federal Awards

Internal control over major programs:		
Material weakness (es) identified?	___ Yes	X No
Significant deficiency (ies) identified?	X Yes	___ No
Type of auditor's report issued on compliance for major programs:	Unqualified opinion	
Any audit findings disclosed that are required to be reported in accordance with section 510 (a) of OMB Circular A-133?	X Yes	___ No

Identification of major programs:

CFDA 93.600 Head Start Program

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

Audited qualified as low-risk auditee?	X Yes	___ No

2. FINDINGS - FINANCIAL STATEMENTS AUDIT

None

3. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAM AUDIT

a. Head Start Program – CFDA No. 93.600

- **Condition 13-1**

The Municipality did not minimize the time elapsed between the transfer of funds from the Agency and disbursements.

Cause

The Municipality did not make disbursements nor reimbursements to the General Fund immediately after receiving the federal funds from the Agency.

Effect

The Municipality is not in compliance with cash management requirement. The internal control procedures are not operating as established.

Criteria

Based on 31 CFR Part 205, the Municipality must minimize the time elapsing between the transfer of funds from the agency and disbursements.

Recommendation

The Municipality should improve the internal control procedures in order to minimize the time elapsed between the transfer of funds and the disbursements.

Questioned Cost

None

- **Condition 13-2**

The Municipality did not report the financial reports on time. The First Funds Request was submitted 11 days after the deadline and the Annual Report was submitted 93 days after the deadline.

Cause

The Municipality managed the federal funds for first time in 2012-2013. In addition, there were personnel changes and the personnel in charge of preparing the reports, had not been hired yet in the Municipality.

Effect

The Municipality is not in compliance with reporting requirements and the signed contract. The Agency cannot verify the operations promptly.

Criteria

Based on Contract 241-2012-000196 from the Family Department and the Northwest Consortium, the First Request should be submitted during the first five labor days after signing the contract, and the Annual Report should be submitted during the 20 days after the program year has ended.

Recommendation

The Municipality should assign personnel to enforce that the financial reports are prepared and submitted on time.

Questioned Cost

None

- **Condition 13-3**

The Annual Report submitted as of February 28, 2013 does not include the Administrative Report.

Cause

The Municipality managed the federal funds for first time in 2012-2013. In addition, there were personnel changes, and the personnel in charge of preparing the reports had not been hired yet in the Municipality.

Effect

The Municipality cannot evidence the costs of administrating the Program which did not exceed the 15 percent of the annual total program costs.

Criteria

Based on Contract 241-2012-000196 from the Family Department and the Northwest Consortium, octave clause, Administrative Cost Report should Submitted trimestral.

Recommendation

The Municipality should assign personnel to prepare the report as required in the Contract.

Questioned Cost

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, 2013

The Municipality have no prior year findings.

MUNICIPIO DE QUEBRADILLAS

ESTADO LIBRE ASOCIADO DE PUERTO RICO
MUNICIPIO DE QUEBARDILLAS
PROGRAMA DE HEAD START

Head Start

CORRECTIVE ACTION PLAN

October 23, 2013

Cognizant or Oversight Agency for Audit:

Municipality of Quebradillas respectfully submits the following corrective action plan for the year ended June 30, 2013.

Name and address of independent public accounting firm: Ortiz, Rivera, Rivera & Co., Suite 152, PO Box 70250, San Juan, Puerto Rico 00936-7250.

Audit period: Fiscal year ended June 30, 2013

The findings from the June 30, 2013 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

FINDINGS - FEDERAL AWARD PROGRAM AUDITS

Finding 13-1 - Head Start - CFDA No. 93.600

Reportable condition: See condition 13-1

Recommendation:

The Municipality should improve the internal control procedures in order to minimize the time elapsing between the transfer of funds and the disbursements.

Management response:

The Municipality will establish internal control to minimize the time from the receipt of federal funds and disbursement of expenses incurred.

Finding 13-2 - Head Start - CFDA No. 93.600

Reportable condition: See condition 13-2

Recommendation:

The Municipality should assign personnel to enforce the financial reports will be prepared and submitted on time.

Management response:

The Program hasappointed a newaccountant withexperiencein the preparationof thistype of report. In addition, anassistantaccountant was hiredin order toensurethat theinformation is beingpostedmonthlyto meetthe required datesfor filingreports to theACUDEN.

Finding 13-3 - Head Start - CFDA No. 93.600

Reportable condition: See condition 13-3

Recommendation:

The Municipality should assign personnel in order to prepare the report as required on the Contract.

Management response:

The Municipalityis receivingtechnicalassistancefrom ACUDEN forthe preparation and filingof this report.

If the Cognizant or Oversight Agency for Audit has questions regarding this plan, please call Ms. Clara Crespo Mendez at (787) 895-2900.

Cordially,

Clara Crespo Mendez
Program Director