

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL
AREA DE ARCHIVO DIGITAL

MUNICIPIO DE RINCON
AUDITORIA 2002-2003
30 DE JUNIO DE 2003

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DE ASUNTOS MUNICIPALES
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**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT
(WITH ADDITIONAL REPORTS REQUIRED
UNDER THE OMB CIRCULAR A-133)

FISCAL YEAR ENDED JUNE 30, 2003

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

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Independent Auditors' Report

Mayor and Municipal Legislature
Municipality of Rincón
Rincón, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of Rincon, Puerto Rico, as of and for the year ended June 30, 2003, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in fourth and fifth paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As more fully described in Note G to the financial statements, the Municipality has not determined and recorded in governmental activities an estimate of the total municipal solid waste landfill post closure care costs of a closed solid waste landfill, as required by accounting principles generally accepted in the United States of America. The amount by which this departure would affect the liabilities of the governmental activities is not reasonably determinable.

We were unable to obtain sufficient and competent evidence to support the allocation of restricted cash and cash equivalents in the Commonwealth Legislative Grants Fund and to support the distribution of pooled cash and cash equivalents between the General Fund, Commonwealth Legislative Grants Fund and Other Governmental Funds because of the inadequacy of accounting records and reports, which do not permit the application of adequate alternative procedures.

We were unable to obtain sufficient and competent evidence to support valuation of certain interfund loans from the Commonwealth Legislative Grants Fund to the General Fund because of the inadequacy of accounting records and reports, which do not permit the application of adequate alternative procedures.

In our opinion, except for the effect of not determining and recording the estimate of solid waste landfill post closure care costs in governmental activities and except for the effects of such adjustments, if any, as might have been determined to be necessary had we been able to obtain sufficient evidence to support the allocation of restricted cash and cash equivalents in the Commonwealth Legislative Grants Fund; to support the distribution of pooled cash and cash equivalents between the General Fund, Commonwealth Legislative Grants Fund and Other Governmental Funds and to support valuation of certain interfund loans from the Commonwealth Legislative Grants Fund to the General Fund, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the governmental activities, the General Fund, the Commonwealth Legislative Grants Fund and the aggregate remaining fund information of the Municipality of Rincon as of June 30, 2003, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In addition, in our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Economic Development Administration Grant Fund, the Debt Service Fund and the \$1,660,000 Bond Issuance Fund of the Municipality of Rincon as of June 30, 2003, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note A, the Municipality has implemented a new financial reporting model, as required by the provisions of Governmental Accounting Standards Board ("GASB") Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*; GASB Statement No. 37, *Basic Financial Statements - and Management Discussion and Analysis - for State and Local Governments: Omnibus - an amendment of GASB Statements No. 21 and 34*; GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, GASB Interpretation No. 6 "*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*" and GASB Statement No. 41 *Budgetary Comparison Schedule - Perceptive Differences - an Amendment of GASB Statement No. 34* as of June 30, 2003.

The Management's Discussion and Analysis on pages 3 through 11 and the Budgetary Comparison Schedule – General Fund on page 43 are not a required part of the basic financial statements, but are supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated May 7, 2004 on our consideration of the Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise the Municipality of Rincon's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by US Office of Management and Budget Circular A-133, "*Audits of State, Local Governments, and Non-Profit Organizations*" and is not a required part of the basic financial statements. Such information in that schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.



Rodriguez, Rivera & Toro LLP

MANAGEMENT DISCUSSION AND ANALYSIS

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

On July 1, 2002 the Management of the Municipality of Rincón implemented Statement No. 34 of the Governmental Accounting Standards Board (GASB) "*Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*". As a result of the requirements of such statement, a Management Discussion and Analysis (MD&A) is prepared. The MD&A is designed to introduce the basic financial statements and provide an analytical overview of the financial activities of the Municipality. Since it focus on current year activities, resulting changes and currently known facts, please read it in conjunction with the Municipality's financial statements.

FINANCIAL HIGHLIGHTS

- The assets of the Municipality, on a government-wide basis, exceeded its liabilities at the close of fiscal year 2003 by \$ 8,533,502 (net assets).
- At the close of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$ 4,369,195, an increase of \$ 91,867 in comparison with the prior year.
- The General Fund, on a current financial resources basis, reported an excess of revenues and other financing sources over expenditures and other financing uses of \$ 527,746 and an unreserved fund balance of (\$ 845,418).
- On a budgetary basis, actual revenues exceeded actual expenditures by \$ 184,674.
- The investment in capital assets as of June 30, 2003 was \$9,794,892 (net of depreciation).
- Long term debt decreased to \$ 5,056,682, approximately 25 percent with respect to prior year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Municipality's of Rincón basic financial statements. The Municipality's basic financial statements comprise three components:

- government-wide financial statements
- fund financial statements
- notes to the financial statements.

This report also contains other supplementary information in addition to the basic financial statements themselves.

In the past, the primary focus of local government financial statements has been summarized fund type information on a current financial resources basis. However, with the implementation of Statement No. 34 of the Governmental Accounting Standards Board (GASB Statement No. 34) for June 30, 2003, the new focus is on both the Municipality as a whole (government-wide) and the fund financial statements. Each view provides a different snapshot of the Municipality's finances. The government-wide financial statements, which are new for fiscal year 2003, provide both long-term and short-term information about the Municipality's overall financial status. The fund financial statements, which have been provided in the past, focus on the individual parts of the Municipality's government, reporting the Municipality's operations in more detail than the government-wide statements. Both perspectives (government-wide and fund) allow the user to address relevant questions, broaden the basis of comparison (year-to-year or government-to-government) and enhance the Municipality's accountability.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

Government-Wide Statements

The government-wide statements report information about the Municipality as a whole using accounting methods similar to those used by private-sector companies. The Statement of Net Assets and the Statement of Activities, which are the government-wide statements, include all of the government's assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. These two government-wide statements report the Municipality's net assets and how they have changed. Net assets (the difference between the Municipality's assets and liabilities) is one way to measure the Municipality's financial health, or financial position. Over time, increases or decreases in the Municipality's net assets are an indicator of whether its financial health is improving or deteriorating. Other non-financial factors such as the condition of the Municipality's roads and other infrastructure may need to be considered to assess the overall health of the Municipality.

Fund Financial Statements

The format of the fund financial statements will be more familiar to traditional users of government financial statements. The fund financial statements provide more detailed information about the Municipality's most significant funds – not the Municipality as a whole. Funds are accounting mechanisms that the Municipality uses to keep track of specific sources of funding and spending for particular purposes. Some funds are required by Federal and Commonwealth regulations, as well by bond covenants. The Municipality's basic services are included in governmental funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances remaining at year-end that are available for spending. Consequently, the governmental fund statements provide a detailed short-term view that helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the Municipality's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, additional information is provided on a subsequent page that explains the relationship (or differences) between the government-wide and fund statements.

The Total Governmental Funds column requires reconciliation because of the different measurement focus from the government-wide statements (current financial resources versus total economic resources) which is reflected on the page following each statement. The flow of current financial resources will reflect bond proceeds and interfund transfers as other financing sources as well as capital expenditures and bond principal payments as expenditures. The reconciliation will eliminate these transactions and incorporate the capital assets and long-term obligations (bonds and others) into the Governmental Activities column of the government-wide statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

This is the first year that the Municipality has presented its financial statements under the new reporting model required by GASB Statement No. 34. This reporting model changes significantly both the recording and presentation of financial data. However, under this statement, the Municipality is not required to restate prior periods for the purposes of providing comparative information. In future years, when prior year information becomes available, a comparative analysis of government-wide information will be included in this report.

Net assets

TABLE 1

**Condensed Statement of Net Assets
June 30, 2003**

Assets	
Current and other assets	\$ 6,159,684
Capital assets	9,794,892
Total assets	<u>\$ 15,954,576</u>
Liabilities	
Current and other liabilities	\$ 2,364,392
Long term liabilities	5,056,682
Total liabilities	<u>7,421,074</u>
Net assets	
Invested in capital assets, net of related debt	8,624,722
Restricted	3,647,342
Unrestricted	(3,738,562)
Total net assets	<u>\$ 8,533,502</u>

Net assets (assets over liabilities) may serve over time as a useful indicator of a government's financial position. The largest portion of the Municipality's net assets reflects its investment in capital assets (e.g., land, buildings, equipment, and infrastructure); less accumulated depreciation and less any related outstanding debt used to acquire those assets. The Municipality uses these assets to provide services to its citizens and consequently, these assets are not available for future spending. The resources needed to repay the debt related to these capital assets must be provided from other sources, because capital assets are not generally liquidated for the purpose of retiring debt. Approximately 43% of the Municipality's net assets are subject to external restrictions.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

Unrestricted net assets are the part of the net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements. As of June 30 2003 the Municipality presented an unrestricted net assets deficit due primarily to incurred long term obligations such as compensated absences and debts to CRIM for which the Municipality did not provide funding in previous budgets. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation. In addition, operational loans and certain general obligation bonds do not have a related capital asset to be reported as Invested in capital assets, net of related debt section of net assets. Therefore, are reported as part of the unrestricted net assets section.

Changes in net assets

TABLE 2

**Condensed Statement of Activities
Fiscal year ended June 30, 2003**

Program revenues:	
Fees, fines and charges for services	\$ 1,338,368
Operating grants and contributions	1,098,261
Capital grants and contributions	2,453,965
General revenues:	
Property taxes	1,770,982
Municipal license taxes	400,253
Grants and contributions not restricted to specific programs	3,539,385
Interest	88,121
Other	98,961
Total revenues	10,788,296
Expenses:	
General government	4,261,832
Public works and sanitation	1,939,654
Public safety	525,233
Culture and recreation	283,526
Claims and judgments	197,767
Welfare and community development	927,609
Education	240,393
Interest on long term debt	189,168
Total expenses	8,565,182
Change in net assets	2,223,114
Net assets-beginning of year	6,310,388
Net assets-end of year	\$ 8,533,502

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

FIGURE 1

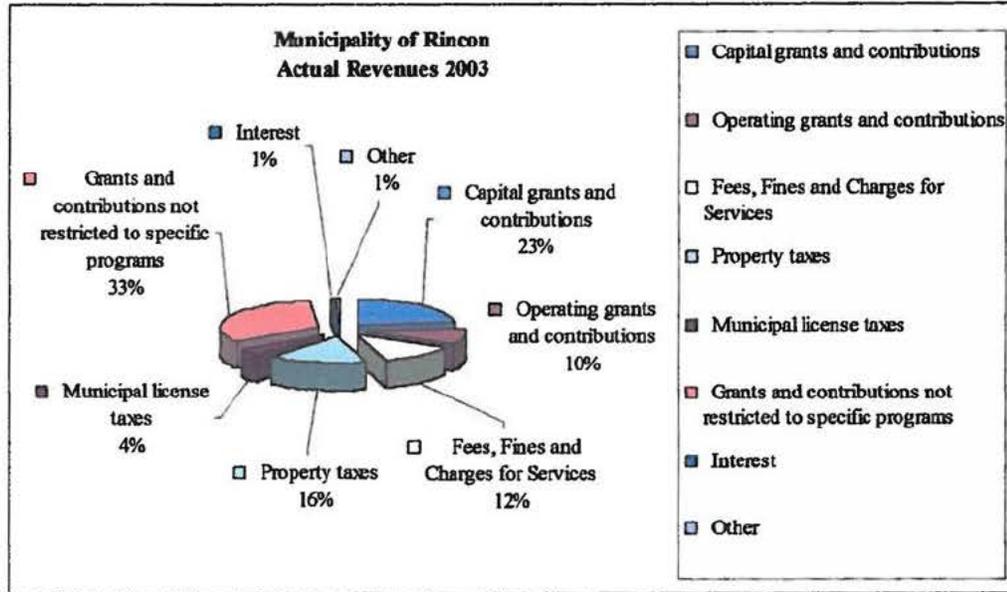
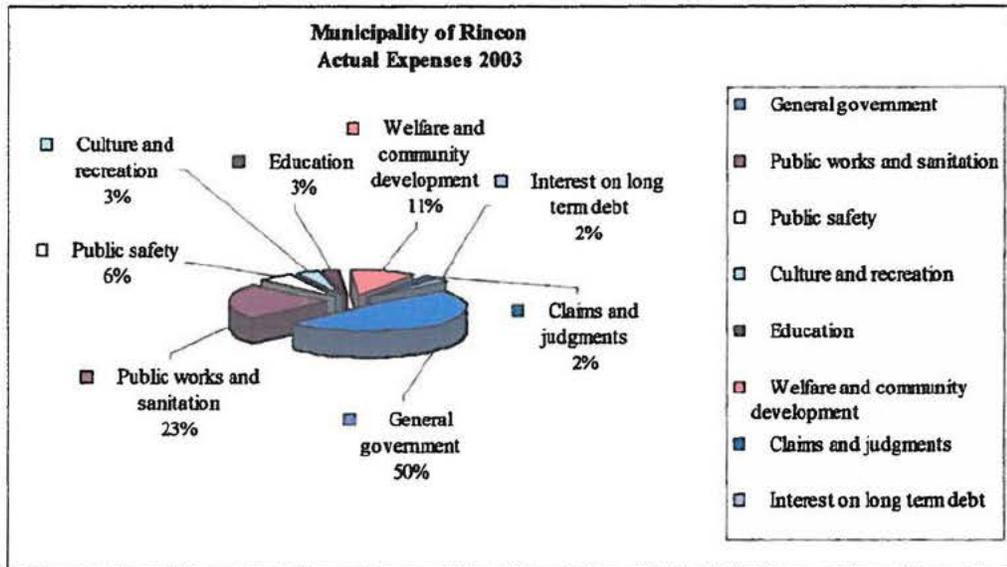


FIGURE 2



Approximately 33% of the Municipality's revenues came from state government contributions 23% comes from donor's imposed contributions. The remaining significant revenues are property taxes with 16%. The Municipality's expenses cover a range of services. The largest expenses are general government representing approximately 50%, public works with 23% and welfare with 11%. Program revenues of the Municipality covered 57% of total expenses.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S FUNDS

Governmental funds

The Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows and balances of resources available for spending. In particular, unreserved fund balance may serve as a useful measure of a Municipality's net resources available at the end of a fiscal year. For the fiscal year ended June 30, 2003, the governmental funds reported combined ending fund balances of \$4,369,195, a net decrease of \$(91,867) in comparison with the prior year. This decrease was caused primarily by a net change (\$246,910) in \$1,660,000 Bond Issuance Fund, (\$263,285) in the Debt Service Fund and (\$181,225) in the other governmental funds. Of total combined fund balances of \$4,369,195, \$5,214,613 is restricted for specific purposes. The remaining fund balance constitutes a deficit, (\$845,418), which pertains to the general fund.

General fund budgetary highlights

The general fund original budget for the fiscal period 2002-2003 presented an increase of 9% with respect to prior year budget. Amendments to the original budget are approved by the Municipal Legislature. During the fiscal year budget revenues were increased by \$130,484 due to additional collections for property taxes. Actual revenues exceeded the revised budgeted revenues by \$145,636 and actual expenditures are less than budgetary appropriations by \$39,038.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets

At the end of the fiscal year, the Municipality has invested \$9,794,892 in a broad range of capital assets, including buildings, parks, roads, bridges, land and equipment. This amount represents a net increase of approximately 27% over the prior year.

TABLE 3

**Municipality of Rincon's Capital Assets
(net of depreciation)
June 30, 2003**

Non-depreciable assets:	
Land	\$ 2,060,668
Construction in progress	1,831,402
Depreciable assets:	
Buildings and buildings improvements	2,122,212
Infrastructure	1,413,788
Vehicles, machinery and equipment	2,366,822
	<hr/>
Total	\$ 9,794,892

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

Capital assets- continued

The most significant projects and costs as of June 30, 2003 were as follow:

- Improvements to City Hall - \$ 655,162
- Improvements to "Plaza de Recreo" - \$ 410,319
- Construction of "Plaza de Bellos Atardeceres" - \$397,373

Long term debt

At year-end, the Municipality had \$3,926,000 in general and special bonds and notes, a increase of 7% with respect to prior year. The Municipality is required to maintain a legal debt margin of 10% of the total assessment of property located within the Municipality plus the balance of the property taxes in the debt service fund.

TABLE 4

**Municipality of Rincón's Outstanding Debt
June 30, 2003**

General and special obligation bonds and notes	\$ 3,926,000
Compensated absences	581,873
Claims and judgments	246,173
Puerto Rico Department of Labor – unemployment payment plan	293,395
Payable to CRIM – property tax advances	470,663
Payable to CRIM – prior years doubtful accounts	165,479
Payable to Dept. of Treasury – property tax advances	61,765
Christmas Bonus	167,418
Total	\$ 5,912,766

More detailed information about the Municipality's long term liabilities is presented in Note F to the financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

MANAGEMENT DISCUSSION AND ANALYSIS

Fiscal year ended June 30, 2003

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Municipality's selected and appointed officials considered many factors when setting the fiscal year 2003-2004 budget. The Municipality applied a conservative approach in development budget estimates. Amounts available for appropriations in the General Fund for the fiscal year 2004 are \$6,407,344 an increase of approximately 4% with respect to prior year estimates. Budgeted expenditures are expected to rise accordingly to the increase of budgeted revenues. The construction industry has been one of the major sources of income generated by the Municipality, in the construction of personal housing, contributing with construction and volume of business taxes for the Municipality.

The Municipality will receive a contribution of \$ 1,200,000 from the Puerto Rico's Commonwealth's government for the construction of the Rincon's City Hall.

CONTACTING FINANCE DIRECTOR

This financial report is design to provide our citizens, taxpayers and customers and creditors with a general overview of the Municipality finances and to show accountability for the money it receives. If you have any questions about this report or need any additional information contact the Finance Department at the Municipality of Rincon, PO Box 97, Rincon, P.R. 00677.

BASIC FINANCIAL STATEMENTS

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

**STATEMENT OF NET ASSETS
JUNE 30, 2003**

	<u>Governmental Activities</u>
ASSETS	
Current assets:	
Cash and cash equivalents (note B)	\$ 86,085
Receivables, net	
Others	155
Due from: (note C)	
Commonwealth Governmental entities	995,111
Federal Government	508,802
Total current assets	<u>1,590,153</u>
Noncurrent assets:	
Restricted assets: (note B)	
Cash and cash equivalents	2,453,009
Cash with fiscal agent	2,093,595
Deferred charges, net	22,927
Capital assets (note E):	
Nondepreciable assets:	
Land and construction in progress	3,892,070
Depreciable assets:	
Buildings, infrastructure, equipment and other	5,902,822
Total capital assets, net	<u>9,794,892</u>
Total noncurrent assets	<u>14,364,423</u>
Total assets	<u>\$ 15,954,576</u>

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

**STATEMENT OF NET ASSETS
JUNE 30, 2003**

LIABILITIES	<u>Governmental Activities</u>
Current liabilities:	
Accounts payable	\$ 523,742
Accrued payroll taxes and withholdings	23,384
Due to: (note C)	
Commonwealth Governmental entities	126,642
Federal Government	24,655
Matured bonds and notes payable	335,000
Matured interest payable	84,909
Current portion of long-term obligations (note F):	
Bonds and notes payable	392,000
Compensated Absences	359,071
Claims and judgments	144,275
Unemployment tax	160,033
Advances from CRIM	7,732
Doubtful accounts-CRIM	5,516
Property taxes-PR Department of Treasury	10,015
Christmas Bonus	167,418
Total current liabilities	<u>2,364,392</u>
Noncurrent liabilities:	
Deposits payable	78,690
Deferred revenues:	
Municipal license taxes (note I)	272,222
Intergovernmental-Commonwealth agencies (note C)	14,292
Federal grants	24,772
Long term liabilities (note F) :	
Bonds and notes payable	3,534,000
Compensated Absences	222,802
Claims and judgments	101,898
Unemployment tax	133,362
Advances from CRIM	462,931
Doubtful accounts-CRIM	159,963
Property taxes-PR Department of Treasury	51,750
Total noncurrent liabilities	<u>5,056,682</u>
Total liabilities	7,421,074
NET ASSETS	
Invested in capital assets, net of related debt	8,624,722
Restricted for:	
Debt service	96,265
Capital projects	3,116,384
Other purposes	434,693
Unrestricted (deficit)	(3,738,562)
Total net assets	<u><u>\$ 8,533,502</u></u>

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

**STATEMENT OF ACTIVITIES
FISCAL YEAR ENDED JUNE 30, 2003**

Functions	Expenses	Program Revenues			Net (expense) revenue and changes in net assets
		Fees, Fines and Charges for services	Operating Grants and Contributions	Capital Grants and Contributions	
Governmental Activities:					
General government	\$ 4,261,832	\$ 1,338,368	\$ 507,155	\$ 149,110	\$ (2,267,199)
Public works and sanitation	1,939,654	-	7,208	2,079,768	147,322
Public safety	525,233	-	-	-	(525,233)
Culture and recreation	283,526	-	-	-	(283,526)
Education	240,393	-	217,864	-	(22,529)
Welfare and community development	927,609	-	366,034	225,087	(336,488)
Claims and judgments	197,767	-	-	-	(197,767)
Interest on long term debt	189,168	-	-	-	(189,168)
Total primary government	\$ 8,565,182	\$ 1,338,368	\$ 1,098,261	\$ 2,453,965	(3,674,588)
General revenues					
					1,770,982
Property taxes					400,253
Municipal license taxes					3,539,385
Grants and contributions not restricted to specific programs					88,121
Interest					98,961
Other					<u>5,897,702</u>
Total					
Change in net assets					2,223,114
Net assets-beginning					6,310,388
Net assets-ending					<u>\$ 8,533,502</u>

The accompanying notes are an integral part of this statement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2003

	General	Commonwealth Legislative Grants	Economic Development Administration Grant Fund	Debt Service Fund	\$1,660,000 Bond Issuance Fund	Other Governmental Funds	Total Governmental Funds
ASSETS							
Cash and cash equivalents (note B)	\$ 86,085	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 86,085
Receivables, net:							
Others	-	-	-	-	-	155	155
Due from: (notes C and D)							
Commonwealth Governmental entities	737,578	-	-	-	-	257,533	995,111
Federal Government	-	-	317,899	-	-	190,903	508,802
Other funds	419,618	-	-	-	-	-	419,618
Advances to other funds (note D)	-	694,758	-	-	-	5,000	699,758
Restricted assets: (note B)							
Cash and cash equivalents	18,009	2,335,789	77,778	-	-	21,433	2,453,009
Cash with fiscal agents	151,591	-	-	516,174	1,405,589	20,241	2,093,595
Total assets	\$ 1,412,881	\$ 3,030,547	\$ 395,677	\$ 516,174	\$ 1,405,589	\$ 495,265	\$ 7,256,133
LIABILITIES							
Accounts payable	\$ 189,784	\$ 5,580	\$ 301,873	\$ -	\$ -	\$ 26,505	\$ 523,742
Accrued payroll taxes and withholdings	23,384	-	-	-	-	-	23,384
Matured bonds and notes payable	-	-	-	335,000	-	-	335,000
Matured interest payable	-	-	-	84,909	-	-	84,909
Due to:							
Commonwealth Governmental entities	113,637	-	-	-	-	-	113,637
Federal Government	24,655	-	-	-	-	-	24,655
Other funds	-	-	-	-	-	419,618	419,618
Advances from other funds	699,758	-	-	-	-	-	699,758
Deposits payable	78,690	-	-	-	-	-	78,690
Deferred revenues:							
Municipal license taxes (note I)	272,222	-	-	-	-	-	272,222
Intergovernmental-Commonwealth agencies (note C)	272,259	-	-	-	-	14,292	286,551
Federal grants	-	-	-	-	-	24,772	24,772
Total liabilities	1,674,389	5,580	301,873	419,909	-	485,187	2,886,938
FUND BALANCES							
Reserved for:							
Debt service	-	-	-	96,265	-	-	96,265
Capital projects	-	3,024,967	93,804	-	1,405,589	17,854	4,542,214
Other purposes	583,910	-	-	-	-	(7,776)	576,134
Unreserved, undesignated, reported in:							
General fund	(845,418)	-	-	-	-	-	(845,418)
Total fund balances	(261,508)	3,024,967	93,804	96,265	1,405,589	10,078	4,369,195
Total liabilities and fund balances	\$ 1,412,881	\$ 3,030,547	\$ 395,677	\$ 516,174	\$ 1,405,589	\$ 495,265	\$ 7,256,133

The accompanying notes are an integral part of this statement.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

**RECONCILIATION OF TOTAL GOVERNMENTAL FUND BALANCE
TO NET ASSETS OF GOVERNMENTAL ACTIVITIES
JUNE 30, 2003**

Total governmental fund balances:		\$	4,369,195
 Amounts reported for governmental activities in the Statement of Net Assets different because:			
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds:			9,794,892
Assets are not available to pay for current period expenditures and therefore are not considered in the funds:			
Deferred charges			22,927
Other assets are not available to pay for current-period expenditures and therefore are deferred in the funds:			
Due from Commonwealth entities:			
Puerto Rico Electric Power Authority (PREPA)	\$	62,962	
CRIM-current year property tax advances liquidation		131,529	
Puerto Rico Department of Treasury-Christmas bonus reimbursemen		<u>77,768</u>	272,259
Long term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds:			
General obligation bonds and notes	\$	3,926,000	
Compensated absences		581,873	
Claims and judgments		246,173	
Puerto Rico Department of Labor-unemployment tax (payment plan)		293,395	
Advances from CRIM (Law No. 42)		470,663	
CRIM-property taxes doubtful accounts		165,479	
Puerto Rico Department of Treasury-Property Taxes		61,765	
Christmas bonus		<u>167,418</u>	(5,912,766)
Other liabilities-due to governmental entities (unemployment tax) that are not due and payable in the current period and therefore are not reported in the funds:			(13,005)
Net assets of governmental activities:		\$	<u>8,533,502</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES-
GOVERNMENTAL FUNDS
FISCAL YEAR ENDED JUNE 30, 2003

	General	Commonwealth Legislative Grants	Economic Development Administration Grant Fund	Debt Service Fund	\$1,660,000 Bond Issuance Fund	Other Governmental Funds	Total Governmental Funds
Revenues							
Property taxes (note H)	\$ 1,456,738	\$ -	\$ -	\$ 314,244	\$ -	\$ -	\$ 1,770,982
Municipal license taxes (note I)	400,253	-	-	-	-	-	400,253
Intergovernmental (note J)							
Commonwealth entities	4,334,167	1,210,200	-	-	-	747,078	6,291,445
Federal grants	-	-	313,899	-	-	1,283,398	1,597,297
Fees, fines and charges for services	531,904	-	-	-	-	-	531,904
Interest	82,718	1,268	58	3,922	-	155	88,121
Other	82,873	-	-	-	-	16,088	98,961
Total revenues	6,888,653	1,211,468	313,957	318,166	-	2,046,719	10,778,963
Expenditures							
Current:							
General government	3,973,667	-	-	158,163	-	744,363	4,876,193
Public works and sanitation	1,745,866	-	-	-	-	-	1,745,866
Public safety	642,740	-	-	-	-	7,210	649,950
Culture and recreation	224,472	-	-	-	-	-	224,472
Welfare and community development	-	365,415	-	-	-	543,143	908,558
Education	-	-	-	-	-	240,302	240,302
Claims and judgments	755,709	-	-	-	-	-	755,709
Capital outlays	-	695,830	392,373	-	246,910	692,926	2,028,039
Debt service							
Principal	-	-	-	364,000	-	-	364,000
Interest	-	-	-	189,168	-	-	189,168
Total expenditures	7,342,454	1,061,245	392,373	711,331	246,910	2,227,944	11,982,257
Excess (deficiency) of revenues over expenditures	(453,801)	150,223	(78,416)	(393,165)	(246,910)	(181,225)	(1,203,294)
Other financing sources (uses)							
Proceeds from general obligation bonds	635,090	-	-	-	-	-	635,090
Proceeds from CRJM - prior years property tax	476,427	-	-	-	-	-	476,427
Operating transfers in	4,127	-	-	134,007	-	-	138,134
Operating transfers out	(134,007)	-	-	(4,127)	-	-	(138,134)
Total other financing sources (uses)	981,647	-	-	129,880	-	-	1,111,427
Net change in fund balance	527,746	150,223	(78,416)	(263,285)	(246,910)	(181,225)	(91,867)
Fund balance at beginning of year, as restated (note K)	(789,254)	2,874,744	172,220	359,550	1,652,499	191,303	4,461,062
Fund balance at end of year	\$ (261,508)	\$ 3,024,967	\$ 93,804	\$ 96,265	\$ 1,405,589	\$ 10,078	\$ 4,369,195

The accompanying notes are an integral part of this statement

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

**RECONCILIATION OF STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FISCAL YEAR ENDED JUNE 30, 2003**

Net change in fund balances-total governmental funds:		\$ (91,867)
Amounts reported for governmental activities in the Statement of activities are different because:		
Governmental funds reports capital assets 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:		
Expenditures for capital assets:	\$ 2,436,930	
Less: current year depreciation	<u>(562,627)</u>	1,874,303
Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds:		
Due from Commonwealth entities:		
Puerto Rico Electric Power Authority (PREPA)-current year	\$ 62,962	
CRIM-current year property tax advances liquidation	131,529	
Puerto Rico Department of Treasury-Christmas bonus reimbursement	<u>77,768</u>	272,259
Revenues reported in funds which are not reported as revenues in the Statement of Activities:		
Due from Commonwealth entities:		
Puerto Rico Electric Power Authority (PREPA)-prior year	\$ (89,193)	
CRIM-prior year property tax advances liquidation	(130,484)	
Puerto Rico Department of Treasury-Christmas bonus reimbursement	<u>(43,249)</u>	(262,926)
Proceeds from general obligation bonds is an other financing source in the governmental funds, but increase long-term liabilities in the Statement of Net Assets		
		(635,000)
Proceeds from CRIM - prior years property tax is an other financing source in the governmental funds, but are not sources of funds in the Statement of Net Assets		
		(476,427)
Expenditures reported in governmental funds are not reported as expenses in the Statement of Activities		
Bond issue costs		3,849
Repayment of long term debt is an expenditure in the governmental funds, but reduces long-term liabilities in the Statement of Net Assets:		
General obligation bonds and notes	\$ 364,000	
Compensated absences	47,752	
Claims and judgments	630,000	
Puerto Rico Department of Labor-unemployment tax (payment plan)	160,033	
Advances from CRIM - prior years debts	484,159	
CRIM-property taxes doubtful accounts	5,516	
Puerto Rico Department of Treasury-Property Taxes	10,015	
Christmas bonus	<u>93,114</u>	1,794,589
Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds:		
Amortization of deferred charges	(3,185)	
Claims and judgments	(72,058)	
Unemployment tax-current period	(13,005)	
Christmas bonus	<u>(167,418)</u>	(255,666)
Change in net assets of governmental activities:		<u>\$ 2,223,114</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Municipality of Rincon was founded in 1770. The Municipality is governed by the executive and the legislative branch elected for a four year term during the general elections in Puerto Rico. The Mayor is the executive officer and the legislative branch consists of twelve (12) members of the Municipal Legislature. The Municipality engages in a comprehensive range of services to the community such as: general government administration, public works, health, environmental control, education, public security, welfare, housing, community development and culture and recreation activities.

The financial statements of the Municipality have been prepared in accordance with accounting principles generally accepted in the United States as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its existing Governmental Accounting and Financial Reporting Standards, which, along with subsequent GASB pronouncements (Statements and Interpretations), constitutes GAAP for governmental units.

In June 1999, the GASB issued Statement No. 34, "*Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*" which affects the way the Municipality prepares and presents financial information. This Statement, which establishes new requirements and a new reporting model for the annual reports of state and local governments, was developed to make annual reports easier to understand and more useful to the people who use the governmental financial information to make decisions.

Other GASB Pronouncements are required to be implemented in conjunction with GASB 34. Therefore, the Municipality has implemented the following GASB Statements in the current fiscal year: GASB Statement No. 37 "*Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus—an amendment of GASB Statements No. 21 and No. 34*"; GASB Statement No. 38 "*Certain Financial Statement Note Disclosures*"; "GASB Interpretation No. 6 "*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*" and GASB Statement No. 41 "*Budgetary Comparison Schedules—Perspective Differences—an amendment of GASB Statement No. 34*."

1. Financial reporting entity

The financial reporting entity included in this report consists of the financial statements of the Municipality of Rincon (primary government). To fairly present the financial position and the results of operations of the financial reporting entity, management must determine whether its reporting entity consists of only the legal entity known as the primary government or one or more organizations called component units. The inclusion of a potential component unit in the primary government's reporting entity depends on whether the primary government is financially accountable for the potential component unit or on whether the nature and significance of the relationship with the primary government is such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. The basic criteria for deciding financial accountability are any one of the following:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

- a. Fiscal dependency of the potential component unit on the primary government, or
- b. The primary government appoints a voting majority of the potential component unit's governing body and
 - 1) The primary government can impose its will on the potential component unit and/or
 - 2) A financial benefit/ burden exist between the primary government and the potential component unit.

There are two methods of presentation of the component unit in the financial statement:

- a. Blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances.
- b. Discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions:

Based on the above criteria there are no potential component units which should be included as part of the financial statements.

2. *Basis of presentation, measurement focus and basis of accounting*

The financial report of the Municipality consists of a Management Discussion and Analysis (MD&A), basic financial statement notes to the financial statements and required supplementary information other than the MD&A. Following is a summary presentation of each, including the measurement focus and basis of accounting. Measurement focus is a term used to describe *which* transactions are recorded within the various financial statements. Basis of accounting refers to *when* transactions are recorded regardless of the measurement focus:

Management Discussion and Analysis

This consists of a narrative introduction and analytical overview of the Municipality financial activities. This analysis is similar to analysis the private sector provides in their annual reports.

Basic financial statements

Basic financial statements include both government-wide and fund financial statements. Both levels of statements categorize primary activities as governmental type, which are primarily supported by taxes and intergovernmental revenues.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Government-wide statements

The government-wide statements consist of a Statement of Net Assets and a Statement of Activities. These statements are prepared using the economic resources measurement focus, which concentrates on an entity or fund's net assets. All transactions and events that affect the total economic resources (net assets) during the period are reported. The statements are reported on the accrual basis of accounting. Revenues are recognized in the period earned and expenses recognized in the period in which the associated liability is incurred. Fiduciary activities, if any, whose resources are not available to finance government programs, are excluded from the government-wide statements. The effect of inter-fund activities is eliminated.

The Statement of Net Assets incorporates all capital (long lived) assets and receivables as well as long term debt and obligations. The Statement of Activities reports revenues and expenses in a format that focus on the net cost of each function of the Municipality. Both the gross and net cost of the function, which is otherwise being supported by the general government revenues, is compared to the revenues generated directly by the function. This Statement reduces gross expenses, including depreciation, by related program revenues, operating and capital grants, and contributions. Program revenues must be directly associated with the function.

The types of transactions included as program revenues are: charges for services, fees, licenses and permits; operating grants which include operating-specific and discretionary (either operating or capital) grants; and capital grants which are capital-specific grants. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes. Property taxes are recognized as revenues in the year for which they are levied. Revenues on both operating and capital grants are recognized when all eligibility requirements (which include time requirements) imposed by the provider have been met. For certain expenditure-driven grants revenue is recognized after allowable expenditures are incurred. As a policy, indirect expenses in the Statement of Activities are not allocated and the Municipality first uses restricted assets for expenses incurred for which both restricted and unrestricted assets are available.

The Municipality reports deferred revenues in the government-wide statements. Deferred revenues arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed and the revenue is recognized.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Fund Statements

The financial transactions of the Municipality are recorded in individual funds, each of which are considered an independent fiscal entity. Each fund is accounted for by providing a separate set of self balancing accounts that comprise its assets, liabilities, reserves, fund equity, revenues and expenditures. Funds are segregated according to their intended purpose which helps management demonstrating compliance with legal, financial and contractual provisions. Governmental Funds are those through which most governmental functions of the Municipality are financed. The governmental fund statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances with one column for the general fund, one for each major fund and one column combining all non-major governmental funds. Major funds are determined based on a minimum criterion (percentage of the assets, liabilities, revenues or expenditures) or based on the Municipality's official's criteria, if the fund is particularly important to financial statement users.

The Municipality reports the following major governmental funds:

General Fund: The General Fund is the general operations fund of the Municipality. It is used to account for all financial resources except those required to be accounted in another fund.

Commonwealth Legislature Grants Fund: This fund accounts for revenue sources from grants provided by the Commonwealth Legislature for specific purposes which includes, among others, acquisition, development and improvements of capital assets.

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

Economic Development Administration Grant Fund: Economic Development Administration Grant Fund is used to account for the financial resources used for the construction of a capital asset.

\$1,660,000 Bond Issuance Fund: This fund is used for improvement and construction of Municipality's new city hall.

Governmental funds are accounted for using the current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are included on the balance sheet in the funds statements. Long-term assets and long-term liabilities are included in the government-wide statements. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets. The fund statements are maintained and reported on the modified accrual basis of accounting. Under this method 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 Municipality 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 the related liability is incurred.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Property taxes are recognized as revenues in the year for which they are levied. Revenues on intergovernmental grants are recognized when all eligibility requirements (which include time requirements) imposed by the provider have been met and revenue becomes available. For certain expenditure-driven grants revenue is recognized after allowable expenditures are incurred. Licenses and permits, charges for services, rent and miscellaneous revenues are recorded as revenues when received because they are not measurable and available.

The Municipality reports deferred revenues in the governmental funds statements which arise when potential revenue does not meet both measurable and available criteria for recognition in the current period (in the government-wide statements revenue is recognized as soon as it is earned regardless of its availability). Deferred revenues also arise when resources are received before the Municipality has a legal claim to them or before applicable eligibility requirements are met. (in case of certain federal expenditure-driven grants if resources are received before allowable expenditures are incurred). In subsequent periods, when the revenue recognition criteria is met, or when the Municipality has a legal claim to the resources, the liability for deferred revenues is removed from the combined balance sheet and the revenue is recognized.

Expenditures are generally recognized when the related liability is incurred. Certain exceptions to this fundamental concept include the following: 1) payments of principal and interest on general long term debt, which are recorded as expenditures when due, except for principal and interest due on July 1 (in this case amounts are recorded as liabilities and expenditures on June 30 since amounts have been accumulated or transferred to the debt service fund before July 1 payments are made) 2) vested compensated absences, claims and judgments and special termination benefits which are recorded as expenditures only to the extent that they are expected to be liquidated with expendable financial resources (in the government-wide statements the expense and related accrual liability for long term portions of debt must be included).

Since the governmental fund statements are presented on a different measurement focus and basis of accounting than the government-wide statements, reconciliation is necessary to explain the adjustments needed to transform the fund financial statements into the government-wide statements. This reconciliation is part of the financial statements.

Notes to Financial Statements

The notes to financial statements provide information that is essential to a user's understanding of the basic financial statements.

Required Supplementary Information:

Required supplementary information consists of the Budgetary Comparison Schedule – General Fund as required by GASB.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

3. *Cash, cash equivalents and cash with fiscal agent*

Cash and cash equivalents consists of cash on hand, demand deposits and investments with original maturities of three months or less from the date of acquisition. The Municipality follows the practice of pooling cash of all funds except for certain Commonwealth's grants, restricted funds generally held by outside custodians and federal grants. Available pooled cash balance beyond immediate needs is invested in certificates of deposits.

Restricted cash with fiscal agent in the debt service fund consists of the undisbursed balance of property tax collections retained by the Commonwealth of Puerto Rico, which are restricted for the repayment of the Municipality's general and special obligation bonds and notes as established by law. Restricted cash and cash equivalents represent the balance of Federal and Commonwealth's grants deposits. Restricted cash with fiscal agent of the general fund and other governmental funds represent restricted undisbursed proceeds of certain bonds, loans or grants which are maintained in a cash custodian account by GDB.

4. *Receivables and due from governmental entities*

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined upon past collection experience and current economic conditions.

Amounts due from Commonwealth governmental entities in the general fund represents contributions from the Puerto Rico Electric Power Authority (PREPA) for payments in lieu of tax and/or represents amounts due from the Municipal Revenues Collection Center (CRIM) for excess of actual collections over advances of property taxes and amounts of municipal equalization fund ; in other governmental funds represents amounts owed to the Municipality for reimbursement of expenditures incurred on Commonwealth agencies grants. Amounts due from federal government represent amounts owed to the Municipality for the reimbursement of expenditures incurred pursuant to federally funded programs.

5. *Interfund receivables and payables*

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due from/to 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 from/to other funds".

6. *Inventories*

The Municipality purchases gasoline, oil and other expendable supplies held for consumption. The cost of those purchases is recorded as expenditure when incurred in the appropriate fund but the year-end inventory is not recorded in the Statement of Net Assets, as management believes is not significant.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

7. *Capital assets*

Capital assets of the primary government, which include property, plant, equipment and infrastructure, (e.g., roads, bridges, sidewalks, and similar items) are reported in the governmental activities column in the Statement of Net Assets. Capital assets are capitalized at historical cost or estimated historical cost if historical cost is not available. Donated assets are recorded as capital assets at their estimated fair market value at the date of donation. The municipality maintains a threshold level of \$1 or more for capitalizing vehicles, machinery and equipment. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

All capital assets, other than land, are depreciated using the straight-line method over the following useful lives:

<u>Description</u>	<u>Years</u>
Land Improvements	20
Buildings and building improvements	20-50
Infrastructure	20-40
Vehicles, machinery and equipment	5-15

8. *Long-term obligations*

Long-term debt and other long-term obligations, which are reported as liabilities in the governmental activities column in the Statement of Net Assets, consists of general and special obligation bonds, liabilities for compensated absences, claims and judgments, and long-term liabilities to other governmental entities.

9. *Deferred charges*

Bond issuance costs are reported as deferred charges and amortized as required by current standards. Governmental fund types recognize bond issuance costs as expenditures during the current period. Those issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the appropriate fund.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

10. *Compensated absences*

The Municipality's employee accumulates vacation and sick leave based on continuous service. The vacation and sick leave for employees are accumulated on the basis of 2½ days per month of vacation and 1½ days per month of sick pay up to a maximum of 60 days of vacations and 90 days of sick leave. Upon separation from employment the accumulated vacations are liquidated up to the maximum number of days. Accumulated sick pay is liquidated to employees with 10 years or more service up to the maximum number of days. Any excess over 90 days, on sick leave, at December 31 calendar year, are reimbursed. The amount of vacations leave is accrued if earned based on services already performed by employees and if it is probable that will be paid in a future period. The amount of sick leave is accrued based on all vesting and no vesting amounts for which payment is probable and on accumulated benefits as of the fiscal year-end.

The accrual of compensated absences includes estimated payments that are related to payroll. The entire compensated absence liability is reported on the government-wide financial statements. For governmental fund financial statements, the current portion of unpaid compensated absences is the amount that is normally expected to be paid using expendable available financial resources.

11. *Fund balance*

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

- Debt Service: Represents net assets available to finance future debt service payments.
- Capital Projects: Represent amounts to be used for future expenditures for capital projects under contracts and other commitments. These commitments generally will become liabilities in future periods as the projects are completed.
- Other purposes: Represent amounts to be used for future expenditures of Federal and Commonwealth's grants to be used to finance activities other than construction or capital improvement commitments

12. *Interfund transactions*

The Municipality reports certain transactions as operating transfers, which are legally required transfers that are reported when incurred as "Operating transfers-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

13. Risk financing

The Puerto Rico Treasury Department (PRDT) acts as an agent, obtaining and determining the coverage for the municipalities of Puerto Rico. The coverage for the Municipality of Rincon consists of professional, public responsibility, property and theft, auto and fidelity bond coverage.

Insurance policies costs are allocated by PRDT among all the municipalities of Puerto Rico. Payment of the Municipality's insurance premiums is monthly deducted from advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM). Workers compensation insurance is also deducted from the monthly advances by the CRIM. Settled cases have not exceeded insurance coverage for any of the past three years.

14. Use of estimates

The preparation of the basic financial statements in accordance 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 basic financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

15. Future adoption of accounting pronouncements

The GASB has issued the following statements, which the Municipality has not yet adopted:

Statement	To be Adopted in Fiscal year ended,
39 Determining Whether Certain Organizations Are Component Units - an amendment of GASB 34 Statement No. 14	June 30, 2004
40 Deposit and Investment Risk Disclosure - an amendment of GASB Statement No. 3	June 30, 2005
42 Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries	June 30, 2006

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE B - DEPOSITS

The Municipality maintains its cash deposits in commercial banks located in Puerto Rico. Under Commonwealth of Puerto Rico statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal deposit insurance. All securities pledged as collateral by the Municipality are held by the Secretary of Treasury of Puerto Rico in the Municipality's name. The table presented below discloses the level of custody risk assumed by the Municipality based upon how its deposits were insured or secured with collateral at June 30, 2003:

- Category 1:** Insured or collateralized with securities held by the Secretary of Treasury agent's in the Municipality's name.
- Category 2:** Collateralized with securities held by the pledging financial institution's trust department or its agents in the Municipality's name.
- Category 3:** Uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the Municipality's name.

The reported amount and bank balances of deposits with financial institutions as of June 30, 2003 were as follows:

	Category			Carrying amount	Bank balance
	1	2	3		
Deposits in commercial banks	\$ 2,539,094	\$ -	\$ -	\$ 2,539,094	\$ 2,362,064
Deposits in governmental banks	-	-	2,093,595	2,093,595	1,577,421
	<u>\$ 2,539,094</u>	<u>\$ -</u>	<u>\$ 2,093,595</u>	<u>\$ 4,632,689</u>	<u>\$ 3,939,485</u>

Reconciliation to government-wide statement of net assets:

	Unrestricted	Restricted	Total
Cash and cash equivalents - (including a certificate of deposits of \$300,000)	\$ 86,085	\$ 2,453,009	\$ 2,539,094
Cash with fiscal agents	-	2,093,595	2,093,595
	<u>\$ 86,085</u>	<u>\$ 4,546,604</u>	<u>\$ 4,632,689</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE C - DUE FROM (TO) GOVERNMENTAL ENTITIES

1. Amounts due from governmental entities as of June 30, 2003 follows:

	Commonwealth Entities	Federal Government
Municipal Revenue Collection Center (CRIM) – excess of actual property tax collections over advances of property tax and amounts of municipal equalization fund	\$ 131,528	\$ -
Puerto Rico Electric Power Authority (PREPA) – compensation in lieu of tax of \$62,962 and \$432,320 on lawsuit final settlement	495,282	-
Puerto Rico Department of Education	33,000	-
Office of Governor’s Authorized Representative (GAR) - FEMA	-	2,349
Office of Commissioner of Municipal Affairs - CDBG	-	73,221
Puerto Rico Department of Family – Child Care	-	115,333
US Department of Commerce-EDA	-	317,899
Rural Development Corporation (CDR)	21,429	
Puerto Rico Department of Treasury – Christmas bonus reimbursement	77,768	-
Puerto Rico Department of Labor – Law No. 52	236,104	-
	\$ 995,111	\$ 508,802

The amounts due from CRIM (\$131,528), PREPA for compensation in lieu of tax (\$62,962) and Puerto Rico Department of Treasury (\$77,768) for a total amount of **\$272,259** are recorded as deferred revenue in the governmental funds statements (general fund) since are not available as required by current standards.

2. Amounts due to governmental entities as of June 30, 2003 follows:

	Commonwealth Entities	Federal Government
Puerto Rico Aqueduct and Sewer Authority (PRASA)	\$ 8,919	\$ -
Office of Governor’s Authorized Representative (GAR) - FEMA	-	24,655
Employee’s Retirement System of the Government of Puerto Rico	30,593	-
Puerto Rico Department of Labor – unemployment benefits paid in behalf of the Municipality	87,130	-
	\$ 126,642	\$ 24,655

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE D - INTERFUND TRANSACTIONS

1. Due from/to other funds:

Amounts due from/to other funds represent temporary advances to other funds by the general fund payroll and payroll taxes expenditures, as follows:

Receivable Fund	Payable Fund	Amount
General Fund	Other governmental funds-CDBG	\$ 46,741
	Other governmental funds-Law No. 52	236,074
	Other governmental funds-Child Care	115,333
	Other governmental funds-CDR	21,429
	Other governmental funds-other	41
		<u>\$ 419,618</u>

2. Advances to other funds

Advances to other funds by the Commonwealth Legislative Grants Fund and Other Governmental Funds in the amount of \$699,758 represents loans made to the general fund for payments of payrolls, payroll taxes and other operational expenditures in previous periods not reimbursed as of fiscal year-end.

3. Operating transfers:

The \$138,134 transfers among individual funds were made for operational purposes. Transfers includes, (1) interest earned on cash with fiscal agents in the debt service fund which is transferred to the general fund; (2) principal and interest payments of long term debt transferred from the general fund to the debt service fund.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

Fiscal year ended June 30, 2003

NOTE E - CAPITAL ASSETS

Capital assets and depreciation activity of the primary government as of and for the year ended June 30, 2003 is as follows:

	Balance July 1, 2002	Increases	Decreases	Balance June 30, 2003
<u>Governmental activities:</u>				
Capital assets, not being depreciated:				
Land	\$ 1,878,825	\$ 181,843	\$ -	\$ 2,060,668
Construction in progress	-	1,831,402	-	1,831,402
Total capital assets not being depreciated:	1,878,825	2,013,245	-	3,892,070
Capital assets, being depreciated:				
Buildings and building improvements	3,830,456	-	-	3,830,456
Infrastructure	4,037,214	-	-	4,037,214
Vehicles, machinery and equipment	4,214,141	631,325	-	4,845,466
Total capital assets being depreciated	12,081,811	631,325	-	12,713,136
Less accumulated depreciation for:				
Buildings and building improvements	(1,629,668)	(78,576)	-	(1,708,244)
Infrastructure	(2,506,865)	(116,561)	-	(2,623,426)
Vehicles, machinery and equipment	(2,111,154)	(367,490)	-	(2,478,644)
Total accumulated depreciation	(6,247,687)	(562,627)	-	(6,810,314)
Total capital assets being depreciated, net	5,834,124	68,698	-	5,902,822
Governmental activities capital assets, net	\$ 7,712,949	\$ 2,081,943	\$ -	\$ 9,794,892

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE E - CAPITAL ASSETS - continued

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

Governmental activities:	
General government	\$ 35,409
Public works and sanitation	345,878
Public safety	79,632
Culture and recreation	71,539
Welfare and community development	24,320
Education	<u>5,849</u>
 Total depreciation expense, governmental activities	 <u><u>\$ 562,627</u></u>

NOTE F - LONG TERM DEBT

1. Summary of long-term debt activity

The following summarizes activity in long-term debt of the primary government for the fiscal year ended June 30, 2003:

	Balance at July 1, 2002	Increases	Decreases	Balance at June 30, 2003	Due within one year
General, Special Obligations Bonds and Notes	\$ 3,655,000	\$ 635,000	\$ (364,000)	\$ 3,926,000	\$ 392,000
Compensated absences	629,624	-	(47,751)	581,873	359,071
Claims and judgments	804,115	72,058	(630,000)	246,173	144,275
Puerto Rico Department of Labor - (unemployment tax)	453,428	-	(160,033)	293,395	160,033
Advances from CRIM	954,822	-	(484,159)	470,663	7,732
Payable to CRIM-prior years doubtful accounts	170,995	-	(5,516)	165,479	5,516
Puerto Rico Department of Treasury - Property Taxes	71,780	-	(10,015)	61,765	10,015
Christmas Bonus	93,114	167,418	(93,114)	167,418	167,418
	<u>\$ 6,832,878</u>	<u>\$ 874,476</u>	<u>\$ (1,794,588)</u>	<u>\$ 5,912,766</u>	<u>\$ 1,246,060</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE F - LONG TERM DEBT - Continued

2. General and special obligation bonds and notes

The Municipality's outstanding general and special obligation bonds and notes at June 30, 2003 amount to \$3,926,000. All these bonds are serviced by the Governmental Development Bank of Puerto Rico (GDB) maturing at various dates. As required by law, the Commonwealth Government is obligated to levy and collect property taxes for payment of principal and interest on bonds and notes. A debt service fund has been established for the bonds and notes at GDB with the proceeds of those property taxes, whereby sufficient funds must be set aside in order to cover the projected debt service requirement, before any new bonds are issued. The Municipality is required to maintain a legal debt margin of 10% of the total assessment of property located within the Municipality plus the balance of the property taxes in the debt service fund. Principal and interest payments of long term debt issued for operational purposes are made through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM).

A detail of the general and special obligation bonds and notes as of June 30, 2003 follows:

	<u>Outstanding Amount</u>
2000 special obligation bonds of \$910,000 due in annual installments of \$75,000 to \$125,000 through July 1, 2010; with interest ranging from 5.0% to 8.0%	\$ 700,000
2002 special obligation bonds of \$635,000 due in annual installments of \$10,000 to \$50,000 through January 1, 2027; with interest at 6.5%	630,000
1996 general obligation bonds of \$75,000 due in annual installments of \$10,000 through July 1, 2005; with interest ranging from 6.5% to 8.0%	20,000
2001 general obligation notes of \$465,000 due in annual installments of \$95,000 to \$ 105,000 through July 1, 2006; with interest ranging from 2.8% to 3.21%	300,000
1999 general obligation notes of \$705,000 due in annual installments of \$140,000 through January 1, 2004; with interest at 2.8%	140,000
1994 public improvement bonds of \$721,000 due in annual installments of \$27,000 to \$52,000 through January 1, 2017; with interest at 5.0%	531,000
2002 general obligation bond of \$1,660,000 due in annual installments of \$30,000 to \$130,000 through July 1, 2026; with interest rates ranging from 2.8% to 5.6%	<u>1,605,000</u>
Total	<u>\$ 3,926,000</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE F - LONG TERM DEBT - Continued

The debt services requirements to amortize general and special obligation bonds and notes as of June 30, 2003 follows:

June 30	Principal	Interest
2004	\$ 392,000	\$ 207,075
2005	268,000	200,917
2006	275,000	187,366
2007	186,000	173,197
2008	193,000	161,256
2009-2013	770,000	627,808
2014-2018	657,000	446,297
2019-2023	640,000	276,270
2024-2027	545,000	71,945
Totals	\$ 3,926,000	\$ 2,352,131

3. Other long-term liabilities

	Amount
Compensated absences - includes accrued vacations, sick leave benefits and other benefits with similar characteristics, represents the Municipality's commitment to fund such costs from future operations. Amount is paid with unrestricted funds	\$ 581,873
Claims and judgments - represent the final settlements of certain legal cases paid subsequent to June 30, 2003 and one case on which the legal counselor expect an unfavorable outcome. A total amount of \$141,441 will be covered with \$910,000 operational loan funds and the remaining balance with unrestricted funds.	246,173
Puerto Rico Department of Labor - payment plan for unemployment benefits paid by the Commonwealth of Puerto Rico in behalf of the Municipality	293,395
Advances from CRIM - represents the balance owed to CRIM at June 30, 2003 for excess of advances of property tax and other subsidies over final amount of property tax collections for the fiscal year ended June 30, 2000. This amount will be repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM).	470,663

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE F - LONG TERM DEBT - Continued

	<u>Amount</u>
Payable to CRIM - prior year's doubtful accounts - As of June 30, 2002 the Municipality has entered into an agreement with the Municipal Revenue Collection Center (CRIM) to refinance the prior year's property tax doubtful accounts, which amounted to \$170,995 on a long-term basis under the provision of Law No. 146 of October 11, 2001. The refinancing was done through a special loan to be repaid from .48% of the net increase of subsidy provided by the Commonwealth of Puerto Rico's general fund. The financing agreement was authorized by the Municipal Legislature of Rincon on Resolution No. 45 of March 27, 2002.	165,479
Puerto Rico Treasury Department - represent advances of property taxes paid in prior years to the Municipality in excess of actual property tax revenues. This amount is currently being repaid with unrestricted funds through withholdings from the advances of property tax and amounts of municipal equalization fund send to the Municipality by the Municipal Revenue Collection Center (CRIM).	61,765
Christmas Bonus - represent the accrued portion corresponding to fiscal year 2002-2003 of the Christmas bonus to be paid in December 2003	<u>167,418</u>
Totals	<u>\$ 1,986,766</u>

NOTE G - LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS OBLIGATIONS

The Municipality discontinued the operation and ceased to accept solid waste in its landfill. Commonwealth's and Federal laws and regulations require the Municipality to perform certain closure procedures and establish monitoring and maintenance procedures at the landfill site for thirty years after closure. The closure procedures were assumed and completed by the Municipality. The Municipality is required to provide post closure care after the closure is completed. Total post closure care costs has not been determined and accounted as required by accounting principles generally accepted in the United States of America as of June 30, 2003.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE H - PROPERTY TAXES

The Municipal Revenue Collection Center (CRIM) (a state governmental agency) is responsible for the assessment, collection and distribution of real and personal property taxes in accordance with the Municipal Property Tax Law (Law 83 of August, 1995). The tax levied on property is determined by the Municipal Government based on limits established by the Commonwealth Legislature. The tax on personal property is self-assessed by the taxpayer. The assessment is made on a return, which must be filed, with the CRIM by May 15 of each year. Real property is assessed by the CRIM. The tax is general assessed on January 1 on all taxable property located within the Municipality. For personal property the tax is due with the return filed on or before May 15. Taxes on real property may be paid on two equal installments, July 1st and January 1st.

The CRIM advances funds to the Municipality based on an estimate of special governmental subsidies and the property taxes to be levied and which are collected in subsequent periods. This distribution includes advances of property tax and amounts of municipal equalization fund from the Commonwealth government. 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. The CRIM prepares a preliminary settlement not later than three months after fiscal year-end and a final settlement not later than six months after fiscal year-end. If actual collections exceed the advances a receivable from CRIM is recorded. However, if advances exceed actual collections, a payable to CRIM is recorded. A receivable of \$131,528 resulting from the final settlement for fiscal year 2002-2003 is recorded as revenue in the government-wide statements but is recorded as a deferred revenue in the governmental funds statements since is not available as required by current standards.

The CRIM performed an audit of prior year's settlements as of June 30, 2001. As a result of this audit, the Municipality has a payable balance of \$476,395. The difference of \$476,427 between this amount and the amount reported in previous years was reported in the general fund as "Proceeds from CRIM-prior year's property tax" and simultaneously recorded as an expenditure. Debt balance as of June 30, 2003 amounts to \$470,663.

NOTE I - MUNICIPAL LICENSE TAXES

Municipal License taxes are assessed annually by the Municipality to all organizations or entities subject to the tax doing business in the Municipality's location except for entities totally or partially exempt pursuant to certain Commonwealth's statutes. This tax is based generally on volume of business or gross sales as shown in a tax return that should be submitted on or before April 15. During the fiscal year ended June 30, 2003 the tax rates were as follows:

Financial business - 1.50% of gross revenues
Other organizations - .50% of gross revenues

The tax is due in two equal installments on July 1 and January 1 of each fiscal year. Tax revenue is recognized at that moment by the Municipality. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year in the amount of \$272,222 is recorded as deferred revenues.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE J - INTERGOVERNMENTAL REVENUES

Intergovernmental revenues in the General Fund are comprised of the following:

	Amount
CRIM - municipal equalization fund	\$ 2,995,011
Compensation in lieu of tax (\$832,695) and other income (\$432,320) received as a result of a legal settlement from the Puerto Rico Electric Power Authority (PREPA)	1,265,015
Puerto Rico Department of Treasury-Christmas bonus reimbursement	74,141
	\$ 4,334,167

NOTE K - FUND BALANCE RESTATEMENTS

Beginning fund balances of governmental funds has been restated to reflect the correction of errors and recognition of certain assets and liabilities not recorded in previous year. Detail of restatements follows:

	General Fund	Commonwealth Legislative Grants Fund	Economic Development Administration Grant Fund	Other Governmental Funds
Fund balance at beginning of year, as previously reported:	\$ (1,198,935)	\$ 2,844,347	\$ 168,197	\$ 267,013
Adjustments:	409,681	30,397	4,023	(75,710)
Fund balance at end of year, as restated	\$ (789,254)	\$ 2,874,744	\$ 172,220	\$ 191,303

NOTE L - RETIREMENT PLAN

1. Plan description

Regular employees of the Municipality contribute to a cost sharing multiple employer defined benefit retirement plan, administered by the Employee's Retirement System of the Government of Puerto Rico an its Instrumentalities (ERS). ERS covers all regular full time public employees working for the central government, public corporations and the municipalities of Puerto Rico. The system provides retirement pensions, death and disability benefits.

Retirement benefits depend upon age at retirement and number of years of credited service. Disability retirement benefits are available to members of occupational and nonoccupational disabilities. Benefits vest after ten years of plan participation. The system was created under Act 447, approved on May 15, 1951, as amended, and became effective on January 1, 1952. Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE L - RETIREMENT PLAN - Continued

Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation. ERS issues a publicly financial report that includes financial statements and required supplementary information of the Plan, which may be obtained from the ERS.

Law No. 305 of September 24, 1999 amended the Act No. 447 of 1951 and was enacted with the purpose of establishing a new pension program (System 2000). The new pension program became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999 may elect either to stay in the defined benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000 will only be allowed to become members of the new program.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. There will be a pool of pension assets, which will be invested by the System, together with those of the current defined benefit plan. Benefits at retirement age will not be guaranteed by the State government and will be subjected to the total accumulated balance of the savings account. 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 up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. If savings accounts balance is \$10,000 or less at time of retirement, the balance will be distributed by the System to the participant as a lump sum. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not been granted under the new program. The employer contributions (9.275% of the employee's salary) will be used to fund the current plan. Under System 2000 the retirement age is reduced from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

2. Funding policy

The Act 447, as amended, is the authority under which obligations to contribute to the Plan by the Plan members, employers and other contributing entities are established or may be amended. Plan members are required to contribute 5.775% of gross salary up to \$6,600 plus 8.275% of gross salary in excess of \$6,600 except for the Mayor or employee under a supplementation plan, which contributes 8.275% of gross salary. The Municipality is required to contribute 9.275% of gross salary.

The Municipality's actual contribution for the current and the previous two fiscal years, which is equal to the required contribution, follows:

Fiscal year ended:	Law No. 447	System 2000
2003	\$ 114,509	\$ 53,814
2002	\$ 125,832	\$ 47,435
2001	\$ 145,798	N/A

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE M - COMMITMENTS

1. Construction

The Municipality has commitments at June 30, 2003 of approximately \$1,379,784 for design, construction, improvements or renovation of certain municipal facilities.

2. Pledged capital assets

On September 25, 2001 the US Department of Commerce, Economic Development Administration (EDA) approved a \$1,000,000 grant to the Municipality for the construction of a Waterfront Tourism Business Center Sunset Village in the Municipality. The receipt of such grant is conditioned upon compliance with terms and conditions of a grant agreement. As required by the grant agreement, for projects involving acquisition, construction or improvement of a building, the Municipality should agree to declare and furnish to EDA, prior to initial award disbursement, a lien, covenant, or other statement, satisfactory to EDA in form and substance, of EDA's interest in the property acquired or improved in whole or in part with funds made available under this award.

On December 20, 2002 the Municipality signed a deed of a voluntary mortgage in the amount of \$1,000,000 in favor of EDA over a parcel of land on which the project is located. During a 20 years term, the Municipality shall not sell, lease, mortgage or otherwise use of alienate any right to, or interest in the grant property as prohibited by the grant agreement, or use that property for any other purposes than the purposes for which the project was financed by EDA unless prior approval of the Assistant Secretary of the Department is obtained. Upon violation of applicable restrictions, the total amount will become due and payable by the Municipality to EDA.

NOTE N - CONTINGENCIES

1. Federal and State grants

Projects financed by Federal and State Grants are subject to audits by grantors and other governmental agencies in order to determine its expenditures to comply with the conditions of such grants. It is the Municipality's opinion that no additional material unrecorded liabilities will arise from audits previously performed or to perform.

2. Litigations

The Municipality is, at present, a defendant in a number of legal matters that arise in the ordinary course of the Municipality's activities. There are cases whereby the Municipality is a defendant or codefendant that will be covered by insurance, certain cases whereby the legal counsel has not determined an outcome and other cases that will not be covered by insurance. One of the Municipality's legal counsels informed that in one case there is a probability of an unfavorable outcome for a total amount of \$32,675 which is accrued in the government wide statements. In relation with settled cases not to be covered by insurance, the Municipality accrued \$213,498 in the government wide statements. However, it is the opinion of the Municipality and the legal counsel that based on their experience, such actions and the potential liabilities will not impair the Municipality's financial position.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

NOTE O - SUBSEQUENT EVENTS

1. On July, 2003 the Municipality obtained the approval to reprogram \$141,441 of \$150,440 balance as of June 30, 2003 from the Governmental Development Bank of Puerto Rico (GDB) for payment of certain settled legal cases, which were paid in August, 2003. Transactions were approved by the Municipal Legislature through Ordenance No. 1 dated July 2, 2003.
2. Subsequent to June 30, 2003 the Governmental Development Bank of Puerto Rico (GDB) approved a \$1,200,000 line of credit to the Municipality to complete the construction of the new city hall. Interest rates will be variable (LIBOR + 1.25% ranging from 5% to 12% annually) and payable each January 1 and July 1. Repayment will be made in three annual installments ending in fiscal year 2006-2007 and financed with a Commonwealth Legislature Grant (RC no. 1474 of November 9, 2003). Transaction was approved by the Municipal Legislature through Resolution No. 37 dated February 24, 2004.

REQUIRED SUPPLEMENTARY INFORMATION

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FISCAL YEAR ENDED JUNE 30, 2003

	Budgeted amounts		Actual Amounts (Budgetary Basis) (See Note A)	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues				
Property taxes	\$ 1,155,411	\$ 1,285,895	\$ 1,456,738	\$ 170,843
Municipal license taxes	415,000	415,000	400,253	(14,747)
Intergovernmental	3,840,930	3,840,930	3,901,848	60,918
Fees, fines and charges for services	668,000	668,000	531,904	(136,096)
Interest	45,000	45,000	86,845	41,845
Other	60,000	60,000	82,873	22,873
Total revenues	<u>6,184,341</u>	<u>6,314,825</u>	<u>6,460,461</u>	<u>145,636</u>
Expenditures				
General government	3,243,096	3,410,572	3,402,993	7,579
Public works and sanitation	1,718,459	1,755,841	1,745,866	9,975
Public safety	741,488	662,527	642,740	19,787
Culture and recreation	218,478	226,169	224,472	1,697
Claims and judgements	125,709	125,709	125,709	-
Transfers to other funds	137,111	134,007	134,007	-
Total expenditures	<u>6,184,341</u>	<u>6,314,825</u>	<u>6,275,787</u>	<u>39,038</u>
Excess (deficiency) of revenues over expenditures	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 184,674</u>	<u>\$ 184,674</u>

The accompanying notes to required supplemental information are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO BUDGETARY COMPARISON SCHEDULE – GENERAL FUND

June 30, 2003

NOTE A - BUDGET PROCESS AND BUDGETARY BASIS OF ACCOUNTING

The Municipal budget is prepared for General Fund following the requirements of the Municipal Law of 1981 as amended. Although all operating expenses and expenditures are allocated to departmental operating budgets, certain items are not considered to be subject to direct control at the department level. These includes: terminal leave payments, payroll taxes, pension costs, court costs and settlements, telephone and electricity expenses and liability, workers compensation and property insurance premiums. Budget amendments, which require a change in total appropriations of any department, are approved by the Municipal Legislature. Certain budget transfers within the limitations and restriction of the Municipal Law can be approved by the Executive Branch or by the Legislature Branch. The budget is prepared on a budgetary (statutory) basis of accounting which is different from GAAP. Revenues include amounts classified by GAAP as other financing sources and expenditures include encumbrances and amounts classified by GAAP as other financing uses. On a GAAP basis, encumbrances outstanding at year end are reported in the governmental funds statements as a reservation of fund balance since they do not constitute expenditures or liabilities while on a budgetary basis encumbrances are recorded as expenditures of current year. Encumbrance appropriations lapse one year after the end of the fiscal year. Unencumbered appropriations are lapsed at year end.

The presentation of the budgetary data excludes other appropriations such as capital projects, debt service and special revenue funds because projects are funded on a multi-year nature, generally requiring several years to complete or effective budgetary control is alternatively achieved through general obligation bond indentures and legal and contractual grant agreement provisions.

NOTE B - BUDGET TO GAAP RECONCILIATION

The budgetary comparison schedule - general fund, present comparisons of the original and final legally adopted budget with actual data on a budgetary basis. Since accounting principles applied for the purposes of developing data on a budgetary basis differ significantly from those used to present accounting principles generally accepted in the United States, the following budget to GAAP reconciliation is presented:

	<u>Amount</u>
Excess of revenues over expenditures (budgetary basis)	\$ 184,674
Add: Non budgeted items recorded as revenues for financial reporting purposes	1,543,747
Less: Non budgeted items recorded as expenditures for financial reporting purposes	<u>(1,200,675)</u>
Net change in fund balance (GAAP basis)	<u>\$ 527,746</u>

SUPPLEMENTAL INFORMATION

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FISCAL YEAR ENDED JUNE 30, 2003**

<u>Federal Grantor/Pass-Through Grantor Program Title</u>	<u>Federal CFDA Number (Note B)</u>	<u>Pass-Through Grantor's Number (Note C)</u>	<u>Expenditures (Note A)</u>
<u>U.S. Department of Housing and Urban Development</u>			
Major Program:			
Passed through the Office of Commissioner of Municipal Affairs: Community Development Block Grant - State's Program	14.228	FD-53 AB-53	\$ 929,872
Nonmajor program:			
Direct program: Section 8 Housing Choice Vouchers	14.871	N/A	<u>137,706</u>
			1,067,578
<u>U.S. Department of Agriculture</u>			
Nonmajor program:			
Passed through the P.R. Department of Education: Child and Adult Care Food Program	10.558	N/AV	10,928
<u>U.S. Department of Health and Human Services</u>			
Nonmajor program:			
Passed through the P.R. Department of Family - Families and Children Administration: Child Care and Development Block Grant	93.575	12-2000-487	184,202
<u>U.S. Department of Commerce</u>			
Major program:			
Direct program: Grants for Public Works and Economic Development Facilities	11.300	N/A	392,373
<u>U.S. Department of Labor</u>			
Nonmajor program:			
Passed through the Northwestern Consortium: WIA Youth Activities	17.259	2002-000503	45,172
Total federal awards expenditures:			<u>\$ 1,700,253</u>

The accompanying notes are an integral part of this schedule.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

June 30, 2003

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality and is presented on the modified accrual basis of accounting. Expenditures are recognized when the related liability is incurred. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Government and Nonprofit Organizations.

NOTE B - FEDERAL CFDA NUMBER

The Catalog of Federal Domestic Assistance (CFDA) Number is a program identification number. The first two digits identify the federal department or agency that administers the program and the last three numbers are assigned by numerical sequence.

NOTE C - PASS -THROUGH GRANTOR'S NUMBER

State or local government redistributions of federal awards to the Municipality, known as "pass-through awards", should be treated by the Municipality as though they were received directly from the federal government. OMB Circular A-133 requires the schedule to include the name of the pass-through entity and the identifying number assigned by the pass-through entity for federal awards received as a subrecipient. Numbers identified as N/A are not applicable and numbers identified as N/AV are not available.

NOTE D - RECONCILIATION OF EXPENDITURES PRESENTED IN THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS TO THE EXPENDITURES PRESENTED IN THE BASIC FINANCIAL STATEMENTS

Description	Economic Development Administration Grant Fund	Other Governmental Funds
14.228	\$ -	\$ 929,872
14.871	-	137,706
10.558	-	10,928
93.575	-	184,202
11.300	392,373	-
17.259	-	45,172
Total federal awards expenditures	392,373	1,307,880
Total nonfederal awards expenditures	-	920,064
Total expenditures, fund statements	<u>\$ 392,373</u>	<u>\$ 2,227,944</u>

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

Mayor and Municipal Legislature
Municipality of Rincón
Rincón, Puerto Rico

We have audited the financial statements of the Municipality of Rincon as of and for the year ended June 30, 2003, and have issued our report thereon dated May 7, 2004 which is qualified since the Municipality has not determined and recorded in governmental activities an estimate of the total municipal solid waste landfill post closure care costs of a closed solid waste landfill, as required by accounting principles generally accepted in the United States of America; were unable to obtain sufficient and competent evidence to support the allocation of restricted cash and cash equivalents in the Commonwealth Legislative Grants Fund and to support the distribution of pooled cash and cash equivalents between the General Fund, Commonwealth Legislative Grants Fund y Other Governmental Funds; and because were unable to obtain sufficient and competent evidence of certain interfund loans from the Commonwealth Legislative Grants Fund to the General Fund. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Municipality of Rincon's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards*, which are described in item 2003 II-2.

Internal Control over Financial Reporting

In planning and performing our audit, we considered Municipality of Rincon's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect Municipality of Rincon's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as item 2003 II-1 and 2003 II-2.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 2003 II-1 and 2003 II-2 in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses. We also noted other matters involving the internal control over financial reporting that we have reported to management in a separate letter dated May 7, 2004.

This report is intended for the information of the management of the Municipality, Commonwealth and Federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.



Rodriguez, Rivera & Toro LLP

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

Mayor and Municipal Legislature
Municipality of Rincón
Rincón, Puerto Rico

Compliance

We have audited the compliance of Municipality of Rincon with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that is applicable to its major federal programs for the year ended June 30, 2003. Municipality of Rincon's major federal programs are identified in the Summary of Auditor's Results Section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of Municipality of Rincon's management. Our responsibility is to express an opinion on Municipality of Rincon's compliance based on our audit.

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

As described in items **2003 III-2** and **2003 III-3** in the accompanying Schedule of Findings and Questioned Costs, the Municipality of Rincon did not comply with the requirements regarding *matching, level of effort, earmarking, reporting* that are applicable to Grants for Economic Works and Economic Development Facilities program. Compliance with such requirements is necessary, in our opinion, for Municipality of Rincon to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality of Rincon complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended June 30, 2003. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items **2003 III-1, 2003 III-4, 2003 III-5, and 2003 III-6.**

Internal Control over Compliance

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

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, on our judgment could adversely affect the Municipality of Rincon's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 2003 III-1, 2003 III-2, 2003 III-3, 2003 III-4, 2003 III-5, and 2003 III-6.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we considered items 2003 III-2 and 2003 III-3 to be material weaknesses. We noted certain immaterial instances of noncompliance that we have reported to management of the Municipality of Rincon in a separate letter dated May 7, 2004.

This report is intended for the information of the management of the Municipality, Commonwealth and Federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

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Rodriguez, Rivera & Toro LLP

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year ended June 30, 2003

I. Summary of audit results:

Part I - Financial Statements

- | | | |
|--|--|---|
| 1. Type of audit report: | <input type="checkbox"/> Unqualified opinion | <input checked="" type="checkbox"/> Qualified opinion |
| | <input type="checkbox"/> Adverse opinion | <input type="checkbox"/> Disclaimer of opinion |
| 2. Reportable conditions identified that are not considered material weakness: | <input checked="" type="checkbox"/> Yes | <input type="checkbox"/> None reported |
| 3. Reportable conditions reported as a material weakness: | <input checked="" type="checkbox"/> Yes | <input type="checkbox"/> No |
| 4. Material noncompliance disclosed: | <input checked="" type="checkbox"/> Yes | <input type="checkbox"/> No |

Part II - Federal Awards

- | | | |
|---|---|---|
| 1. Reportable conditions reported: | <input checked="" type="checkbox"/> Yes | <input type="checkbox"/> No |
| 2. Reportable conditions identified that are not considered material weakness: | <input checked="" type="checkbox"/> Yes | <input type="checkbox"/> None reported |
| 3. Type of report on compliance for major programs: | <input type="checkbox"/> Unqualified opinion | <input checked="" type="checkbox"/> Qualified opinion |
| | <input type="checkbox"/> Adverse opinion | <input type="checkbox"/> Disclaimer of opinion |
| 4. Audit findings required to be reported under Section 510(a) of OMB Circular A - 133: | <input checked="" type="checkbox"/> Yes | <input type="checkbox"/> No |
| 5. Major programs: | <u>CFDA Number(s)</u> | <u>Name of Federal Program or Cluster</u> |
| | 14.228 | Community Development Block Grant - State's Program |
| | 11.300 | Grants for Economic Works and Economic Development Facilities |
| 6. Dollar threshold used to distinguish Type A and Type B programs: | <input checked="" type="checkbox"/> \$300,000 | |
| 7. Low-risk auditee: | <input type="checkbox"/> Yes | <input checked="" type="checkbox"/> No |

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

II. Findings related to the financial statements reported in accordance with GAGAS:

Reference Number: 2003 II-1
Area: Accounting Records and Reports
Type: Material weakness

Condition and criteria:

The Municipality has not properly implemented and established internal controls and procedures to maintain adequate, complete and reconciled set of accounting records and reports. Our audit revealed the following:

- a. The Municipality has not maintained an adequate general ledger record to post and register its financial transactions. In addition, has not established a complete set of manual accounting records properly balanced and has not established procedures to reconcile with the computerized accounting system. The financial statements has been prepared from other alternative sources, including manual subsidiary records and reports
- b. There are no adequate controls over transactions recording on the Form 4(a) Monthly Cash Report since previous years. Several accounts related to General Fund and Commonwealth's and Federal Grants accounts disclose deficits or inappropriate cash ending balances. This situation is caused by excess and erroneous costs charged, interfund loans or advance payments not reimbursed or adjusted. A complete review of Form 4(a) Cash Report balances is recommended to correct and report appropriate revenues, expenditures and cash cumulative balances.
- c. There are significant amounts included as reconciling items in bank conciliations of General Fund and one account related to Commonwealth's Legislative resolutions. Also, there are unreconciled or significant differences between cash balances in the Form 4(a) Monthly Cash Report with applicable bank reconciliations of CDBG, Local Law Enforcement, Section 8, and Edward Byrne special accounts. Those reconciling items arise primarily from amounts not adjusted in the report, amounts deposited into erroneous bank accounts and accounting errors.
- d. Section 8 program general ledger is not balanced and complete. It does not include accounts related to program fund balance.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

II. Findings related to the financial statements reported in accordance with GAGAS:

Reference Number: 2003 II-1 - continued

Cause and effect:

There is no proper reconciliation procedures to assure adequacy and completeness between different accounting records and reports including general ledger, orders and contracts register, investment register, federal financial assistance program records, bank reconciliations, monthly and annual reports and other financial information maintained by Commonwealth's agencies including the Government Development Bank of Puerto Rico and the Municipal Revenue Collection Center (CRIM). As a result of the inadequacy of accounting records in this area we could not support the allocation of restricted cash and cash equivalents in the Commonwealth Legislative Grants Fund and support the distribution of pooled cash and cash equivalents between the General Fund, Commonwealth Legislative Grants Fund y Other Governmental Funds

Recommendation:

A complete and immediate review of controls and procedures over financial records and reports should be performed by the Municipality in order to provide management with a complete, accurate and reliable set of accounting records and reports. Those procedures should include, at least, the following:

- a. Review of Form 4(a) Monthly Cash Report balances and reconciliation with cash subsidiary records (bank reconciliations).
- b. Reconciliation procedures between accounting records including general ledger and other accounting registers.
- c. Reconciliation of centralized accounting records with federal financial assistance accounting records.
- d. Reconciliation of accounts which information is maintained by Commonwealth's agencies including Governmental Development Bank of Puerto Rico and the Municipal Revenue Collection Center (CRIM).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

II. Findings related to the financial statements reported in accordance with GAGAS:

Reference Number: 2003 II-2
Area: Interfund transactions
Type: Material Weakness, material noncompliance

Condition and criteria: Our tests to interfund transactions disclosed the following:

- (1) The Municipality received from the Commonwealth's Legislature certain grants funds which are restricted for specific purposes. Certain general fund expenditures have been financed with these restricted grants funds, which is not in accordance with grantor's established purposes. During the year \$100,000 were repaid from the general fund but the remaining debt balance has not been determined since the Municipality has not adequate records of funds advanced.
- (2) Since previous years the general fund owed to the Commonwealth's Legislative Grants Funds \$694,738 which were advanced to finance certain operational transactions as follows:
 - \$280,000 paid in June, 2000 to finance payroll expenditures,
 - \$61,780 paid in December, 2000 to finance the Christmas bonus expenditures,
 - \$352,958 paid in January 2, 2001 for payment of a settled legal case.

As of June 30, 2003 the Municipality has not provided funds to repay to the Commonwealth's Legislative Grants Fund the referred advances.

Cause and effect: Since fiscal year 2000-2001 the Municipality has cash flow problems and was not complying with payments to suppliers. Therefore, funds were used from restricted grants to pay operational type expenditures. These advances have been recognized in the financial statements as advances from other funds and comprise a significant part of the general fund's deficit.

Recommendation: The Municipality should avoid payment of operational expenditures with restricted funds and should determine the total debt of the advances to the general fund. A payment plan should be established to eliminate the interfund debt.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

III. Findings and questioned costs related to federal awards:

Reference Number: **2003 III-1**
Agency: **U. S. Department of Housing and Urban Development**
Pass-through Entity: **Office of Commissioner of Municipal Affairs (OCAM)**
Program: **Community Development Block Grant – State’s Program**
CFDA Number: **14.228**
Regulation/Requirement: **Special Tests and Provisions - tests for compliance with materials donation program**
Type: **Reportable Condition, noncompliance with program requirements**
Questioned Costs: **\$ -0-**

Condition and criteria: Our tests to a sample of 7 participants files (from a population of 16 files) of the materials donation program disclosed that the following documents were missing from files:

- a. Evidence of property – 1 case
- b. Copy of ID card – 1 case
- c. Copy of social security card – 3 cases
- d. Evidence of electricity or water utilities receipts – 1 case
- e. Evidence of the receipt of the materials – 6 cases
- f. Final inspection not completed - 6 cases
- g. Follow up visit form was not completed – 7 cases

Program regulations require that these documents should be requested to participants or prepared by Federal Programs Office personnel.

Cause and effect: Established internal controls related to participants files documentation are not been followed by Federal Programs Office personnel.

Recommendation: Personnel of the Federal Programs Office should strictly follow established procedures for requesting and preparation of information to be included in participants files. Information of evidence of materials receipt and use is critical to measure program performance. The internal auditor should perform an audit of participant files to identify and request missing information.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

III. Findings and questioned costs related to federal awards:

Reference Number: 2003 III-2
Agency: U. S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Matching, Level of Effort , Earmarking
Type: Material weakness, Material non compliance with program requirements
Questioned Costs: \$ -0-

Condition and criteria:

The grant agreement between the Municipality and the federal grantor specified a total project cost of \$1,250,000 with a Municipal share of \$250,000. As part of the requirements to grant project funds the Municipality certified to the federal agency that as of July 24, 2001 the corresponding matching funds were committed and available in a restricted funds bank account. The funds available in the bank account correspond to Commonwealth Legislative Grants. Funds for the EDA project were provided as follows:

January 18, 2002: \$173,197
November 20, 2003: 57,132
\$ 230,329

These funds were obtained from Citizens Participation Grants approved by the Commonwealth's government to be used as the Municipal share. As of the date of the bid (December 6, 2002) the remaining municipal share or \$76,803 was not provided and transferred by the Municipality to the EDA bank account. The remaining amount of \$19,671 will be also obtained from a Citizens Participation Grant approved by the Commonwealth's government.

Cause and effect:

As required by grant agreement provisions, matching funds were not provided by the Municipality as of the date of the bid.

Recommendation:

The Municipality should request to the applicable Commonwealth agency the remaining funds to be used for matching avoid to request funds without having funds available for matching.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

III. Findings and questioned costs related to federal awards:

Reference Number: 2003 III-3
Agency: U. S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Reporting
Type: Material weakness, material non compliance with program requirements
Questioned Costs: \$ -0-

Condition and criteria: As stated in the grant agreement between the Municipality and the federal grantor the Municipality is required to submit to the federal agency a financial report that provides information on the amount of allowable project expenses that has been incurred but not claimed for reimbursement as of the end of the reporting period. The report would be as of September 30 of each year and must be submitted annually until the final grant payment is made by EDA. The report should be submitted to EDA no later than October 30 of each year. The referred report have not been prepared and submitted by the Municipality.

Cause and effect: The Municipality has not established applicable procedures to comply with requirement. This is a material instance of non compliance and as stated by grant agreement, may result in the suspension of EDA grant.

Recommendation: The applicable report should be prepared and submitted to the federal agency. Adequate procedures should be established to assure that reports are prepared and submitted as required by grant agreement.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

III. Findings and questioned costs related to federal awards:

<i>Reference Number:</i>	<u>2003 III-4</u>
<i>Agency:</i>	U. S. Department of Commerce
<i>Program:</i>	Grants for Public Works and Economic Development Facilities
<i>CFDA Number:</i>	11.300
<i>Regulation/Requirement:</i>	Davis-Bacon Act
<i>Type:</i>	Reportable condition, noncompliance with program requirements
<i>Questioned Costs:</i>	\$ -0-

Condition and criteria: The Municipality is required to establish and place in operation adequate internal controls to provide reasonable assurance that contractors paid the prevailing wages rates for projects covered by the Davis-Bacon Act. Our tests disclosed that there is no evidence that the Municipality is performing on-site visits to monitor classifications and wage rates.

Cause and effect: The Municipality has not established applicable procedures to comply with requirement.

Recommendation: The Municipality should assign personnel of the federal programs office to perform the on-site visits and obtain applicable compliance requirements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

III. Findings and questioned costs related to federal awards:

<i>Reference Number:</i>	<u>2003 III-5</u>
<i>Agency:</i>	U. S. Department of Commerce
<i>Program:</i>	Grants for Public Works and Economic Development Facilities
<i>CFDA Number:</i>	11.300
<i>Regulation/Requirement:</i>	Procurement, Suspension and Debarment
<i>Type:</i>	Reportable condition, noncompliance with program requirements
<i>Questioned Costs:</i>	\$ -0-

Condition and criteria: The Municipality is required to establish and place in operation adequate internal controls to require each of its contractors employed in the completion of the project to comply with procurement, suspension and debarment policies. There is no evidence of project contractor's certification of compliance with referred requirements.

Cause and effect: The Municipality has not established applicable procedures to comply with requirement.

Recommendation: The Municipality should obtain evidence of contractor's certification of compliance with procurement, suspension and debarment policies and improve compliance controls policies to avoid lack of evidence and documentation of compliance with applicable regulations.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON

SCHEDULE OF FINDINGS AND QUESTIONED COSTS - Continued

Year ended June 30, 2003

III. Findings and questioned costs related to federal awards:

Reference Number: 2003 III-6
Agency: U. S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Special tests and provisions – compliance with other grant agreement requirements
Type: Reportable condition, noncompliance with program requirements
Questioned Costs: \$ -0-

Condition and criteria: The project contractor was obligated to make a documented good faith effort on this project to employ the unemployed/underemployed residents of the Municipality of Rincon. Records should be provided to the Municipality. There is no evidence of compliance with this requirement.

Cause and effect: The Municipality has not established applicable procedures to request to the construction contractor evidence of employment of residents of the Municipality.

Recommendation: The Municipality should obtain evidence of contractor's efforts to employ residents of the Municipality.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year ended June 30, 2003

I. Findings related to the financial statements reported in accordance with GAGAS:

Fiscal year ended June 30,	Finding No.	Condition	Status
1998, 1999,2000, 2001 and 2002	98 II-1; 99 II-1; 2000 II-1; 2001 II-1; 2002 II-1	The Municipality has not established adequate controls and procedures to assure the completeness, existence and valuation of fixed assets inventories.	Finding remains unclear. See current year finding No. 2003 II-2 in the accompanying Schedule of Findings and Questioned Costs.
1998, 1999 and 2000	98 II-2; 99 II-2; 2000 II-2	<ul style="list-style-type: none"> a. Several instances of excess of expenditures over appropriations in the general fund. b. Operational budgetary deficit and cumulative fund balance deficit (GAAP). 	Finding remains unclear.
1997, 1998, 1999,2000, 2001 and 2002	97 II-1; 99 II-3; 2000 II-3; 2001 II-3; 2002 II-2	Failure to properly implement established internal controls and procedures to maintain complete, accurate and reliable set of accounting records and reports.	Finding remains unclear. See current year finding No. 2003 II-1 in the accompanying Schedule of Findings and Questioned Costs.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year ended June 30, 2003

I. Findings related to the financial statements reported in accordance with GAGAS:

Fiscal year ended June 30,	Finding No.	Condition	Status
1997	97 II-2	<p>During our examination of internal controls and procedures over the bid process we noted that there was an awarded bid for a construction project of \$3,082,000 where the appropriated budget was \$2,500,000 to cover the awarded bid costs. As stated on the bid board minutes, the bid was awarded based on the recommendation of the Recreational Development Company of Puerto Rico (a state governmental agency). This recommendation authorized the Municipality to award the bid for the budget amount the Municipality has available with an agreement to obtain the total additional funds within six months. The Municipality decided to contract the construction project in three stages based on availability of funds. The total amount of the three stages was \$2,715,000, which represents \$318,000 above the original estimated construction costs. As stated in communications between the contractor and the Municipality, the excess costs are based on changes in costs for the additional time incurred and extended overhead cost.</p>	Finding remains unclear.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year ended June 30, 2003I. Findings and questioned costs for federal awards:

<u>Fiscal year ended June 30,</u>	<u>Program</u>	<u>Finding Number</u>	<u>Condition</u>	<u>Status</u>
2002	US Department of HUD Community Development Block Grant- State's Program CFDA Number 14.228	2002 III-1	Our tests to a sample of six participant's files of materials donations program financed with SBGP funds disclosed that the certain documents were missing from files.	Finding remains unclear.
2001	US Department of HUD Community Development Block Grant- State's Program CFDA Number 14.228	2001 III-1	In our tests related to procurement procedures we noted that in two bids for asphalt services and in one case related to the acquisition of a vehicle the Municipality could not provide evidence of proper evaluation and criteria for bidder selection.	Finding remains unclear.
2001	US Department of HUD Community Development Block Grant- State's Program CFDA Number 14.228	2001 III-2	Municipalities are required to request from contractors a certification stating that Entity's Principals are not suspended or debarred from doing business with state or Federal Government or this requirement may be included as a contract's clause. During our examination on three of the Municipality's contracts over \$100,000 we noted that in two cases such clauses were not included in contract nor a certification was obtained from contractors.	Finding remains unclear. See related current year Finding No. 2003 III-5 in the accompanying Schedule of Findings and Questioned Costs.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year ended June 30, 2003

II. Findings and questioned costs for federal awards:

Fiscal year ended June 30,	Program	Finding Number	Condition	Status
2000	US Department of HUD Community Development Block Grant- State's Program CFDA Number 14.228	2000 III-1	A service contract not provided for examination.	Finding and related questioned costs of \$548,751 remains unclear.
1999	Federal Emergency Management Agency - Public Assistance Grants CFDA Number 83.544	99 III-1	<ul style="list-style-type: none"> a. In two instances the disbursements were made and no Damaged Survey Report (DSR) has been approved by FEMA. b. In seven instances the disbursement's concept is not in accordance with approved cost category disclosed on DSR. 	Finding remains unclear. Questioned Costs totaled \$17,730.
1999	Federal Emergency Management Agency - Public Assistance Grants CFDA Number 83.544	99 III-2	The Municipality has not complied in one case with suspension and debarment certification.	Finding remains unclear. See related current year Finding No. 2003 III-5 in the accompanying Schedule of Findings and Questioned Costs.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RINCON**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year ended June 30, 2003

II. Findings and questioned costs for federal awards:

<u>Fiscal year ended June 30,</u>	<u>Program</u>	<u>Finding Number</u>	<u>Condition</u>	<u>Status</u>
1997	U.S. Department of HUD: Community Development Block Grant – State’s Program CFDA Number 14.228	97 III-1	During our internal controls tests over the federal funds we found that grantee has not established procedures to comply with suspension and debarment requirement.	Finding remains unclear See related current year Finding No. 2003 III-5 in the accompanying Schedule of Findings and Questioned Costs.

Municipality of Rincón
Findings and Corrective Actions
Year ended June 30, 2003

Reference number: 2003 II-1

Area: Accounting Records and Reports

Type: Material weakness

Recommendation: A complete and immediate review of controls and procedures over financial records and report should be performed by the Municipality in order to provide management with a complete, accurate and reliable set of accounting records and reports. Those procedures should include, at least, the following:

Corrective Actions:

- a. The Finance Department and the controller should coordinate with "OCAM" or professional services for assistance and training of 4A Monthly Cash Report balances and reconciliation with cash subsidiary records.
- b. Training will be continued with OCAM to comply with reconciliation procedures that will include the general ledger and other accounting registers.
- c. The Finance Department will continue to update and centralize the accounting records with federal financial assistance accounting records.
- c. The reconciliation accounts should be better coordinated between agencies, so these accounts are reconciled.

**Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003**

Reference number: 2003 II-2

Area: Interfund transactions

Type: Material weakness, material noncompliance

Recommendation: The Municipality should avoid payment of operation expenditures with restricted funds and should determine the total debt of the advances to the general funds. A payment plan should be established to eliminate the interfund debt.

Corrective Action:

- a. During fiscal years 2000 – 2001 the past administration was irresponsible of these transactions that are identified in this report. As of 2001 this administration has repaid from the general funds on or about \$100,000.00 we are continuing to identify the funds that are owed to the Commonwealth's Legislature Grants fund.
- b. The Municipality will determine the total debt of the advances to the general fund to establish a payment plan to eliminate the interfund debt.

Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003

Reference number: 2003 III-1
Agency: U.S. Department of Housing and Urban Development
Pass-Through Entity: Office of Commissioner of Municipal Affairs (OCAM)
Program: Community Development Block Grant-State's Program
CFDA Number : 14.228
Regulation/Requirement: Special Tests and Provisions – tests for compliance with materials donation program
Type: Reportable Condition, noncompliance with program requirements
Questioned Costs: \$-0-

Recommendation: Personnel of the Federal Programs Office should strictly follow established procedures for requesting and preparation of information to be included in participants files. Information of evidence of materials receipt and use is critical to measure program performance. The internal auditor should perform an audit of participant files to identify and request missing information.

Corrective Action: The Federal Programs Office personnel will strictly follow the established procedures for requesting and preparation of informations of the participants files. No materials will be given to any participants until all documentation are provided to the Federal Programs Office.

**Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003**

Reference number: 2003 III-2
Agency: U.S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Matching, Level of Effort, Earmarking
Type: Material weakness, Material non compliance with program requirements
Questioned Costs: \$-0-

Recommendation: The Municipality should request to the applicable Commonwealth agency the remaining funds to be used for matching avoid to request funds without having funds available for matching.

Correction action: The Municipality had identified and solicited the matching funds, but did not have them available at the time of the bid, because the Commonwealth's Citizens participation Grant Agency delayed the issue of the funds to the Municipality.

**Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003**

Reference number: 2003 III-3
Agency: U.S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Reporting
Type: Material weakness, material non compliance with program requirements
Questioned Costs: \$-0-

Recommendation: The applicable report should be prepared and submitted to the federal agency. Adequate procedures should be established to assure that reports are prepared and submitted as required by agrant agreement.

Correction Action: All EDA report will be prepared and submitted to the Economic Development Administration (ASPA) to comply with grant agreement.

Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003

Reference number: 2003 III-4
Agency: U.S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number : 11.300
Regulation/Requirement: Davis-Bacon Act
Type: Reportable condition, noncompliance with program requirements
Questioned Costs: \$-0-

Recommendation: The Municipality should assign personnel of the federal programs office to perform the on-site visits and obtain applicable compliance requirements.

Correction Action: The Federal Program Office did have personnel auditing the wages rates for projects covered by the Davis-Bacon Act, but did not evidence required visit. This personnel will immediately comply with establish procedures.

Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003

Reference number: 2003 III-5
Agency: U.S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Procurement, Suspension and Debarment
Type: Reportable condition, noncompliance with program requirements
Questioned Costs: \$-0-

Recommendation: The Municipality should obtain evidence of contractor's certification of compliance with procurement, suspension and debarment policies and improve compliance controls policies to avoid lack of evidence and documentation of compliance with applicable regulations.

Corrective Action: The Municipality Secretary Office will immediately comply with establish procedures.

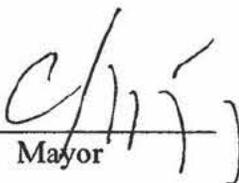
Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003

Municipality of Rincón
Findings and Corrective Actions, Continued
Year ended June 30, 2003

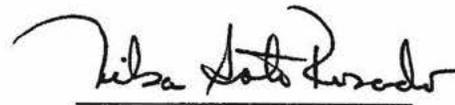
Reference number: 2003 III-6
Agency: U.S. Department of Commerce
Program: Grants for Public Works and Economic Development Facilities
CFDA Number: 11.300
Regulation/Requirement: Special tests and provisions-compliance with other grant agreement requirements
Type: Reportable condition, noncompliance with program requirements
Questioned Costs: \$-0-

Recommendation: The Municipality should obtain evidence of contractor's efforts to employ residents of the Municipality.

Correction Action: The Municipality will request the contractor evidence of efforts of employment of residents of Rincón to completed the project file.



Mayor



Finance Director