

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES

AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE RIO GRANDE

AUDITORIA 2004-2005

30 DE JUNIO DE 2005

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE
SINGLE AUDIT REPORT
YEAR ENDED JUNE 30, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2005

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2005

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Río Grande
Río Grande, 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 Río Grande, Puerto Rico (Municipality)**, as of and for the year ended June 30, 2005, which collectively comprise the **Municipality's** basic financial statements as listed in the table of contents. These financial statements are the responsibility of the **Municipality's** management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Río Grande, Puerto Rico**, as of June 30, 2005, 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.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

The Management's Discussion and Analysis on pages 3 through 12 and the Budgetary Comparison Schedule-General Fund on page 41 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 21, 2005 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of the **Municipality of Río Grande**, taken as whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the respective financial statements. The 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.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 21, 2005

Stamp No. 2106103 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2005

This discussion and analysis of the Municipality of Río Grande (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2005. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2004. This MD & A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

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

FINANCIAL HIGHLIGHTS

The following comments about the financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2005 deserve special mention:

1. Total assets of the Municipality amounted to \$37,898,534 which represents a decrease of 33% compared to prior fiscal year.
2. At the end of fiscal year 2005, total liabilities amounted to \$27,425,234. Out of said amount, \$21,241,050 corresponded to long-term liabilities of which \$15,936,000 represented the outstanding balance of bonds issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.
3. Total net assets of the Municipality amounted to \$10,473,300 which represents a decrease of 65% compared to prior fiscal year;
4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$20,280,560, derived from the following sources: \$63,163 charges for services; \$1,743,577 from operating grants and contributions; \$2,040,093 from capital grants and contributions obtained from other sources, and \$16,433,727 from general revenues available.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL HIGHLIGHTS (CONTINUED)

5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$24,377,599;
6. As reflected in the Statement of Activities, the current fiscal year operations contributed to a decrease in the Net Assets figure by \$4,097,039;
7. As of the close of the current fiscal, the Municipality's Governmental Funds reported combined ending fund balances of \$12,761,371;
8. As the end of the current fiscal year the Municipality's general fund balance amounted to \$1,936,159, compared to a fund balance of \$6,854,967 in the prior fiscal year;
9. The actual General Fund budgetary activities resulted in a favorable balance of \$1,075,878.

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2005. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

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

FINANCIAL STATEMENTS COMPONENTS

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

The Statement of Net Assets reflects information of the Municipality as a whole of a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year. Such financial level is measured as the difference between total assets and liabilities, with the difference between both items reported as net assets. It is important to note that although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations. The higher the increments achieved in net revenues, the higher the capacity to increase the net assets figure either thru additional borrowings or thru internally generated funds. This in turn will benefit the welfare of Río Grande constituents.

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

A brief review of The Statements of Activities of the Municipality at June 30, 2005, shows total expenses incurred to afford the cost of all functions and programs amounted to \$24,377,599. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$3,846,833 was derived from the following sources: \$63,163 charges for services; \$1,743,577 from operating grants and contributions; and \$2,040,093 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$16,433,727. When such figure is added to the \$3,846,833 previously mentioned, total revenues available for the financing of activities amounted to \$20,280,560. There was an excess of expenses over revenues in the amount of \$4,097,039 which contributed with a decrease to the figure of net assets attained at the end of the fiscal year.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

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

INFRASTRUCTURE ASSETS

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

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

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

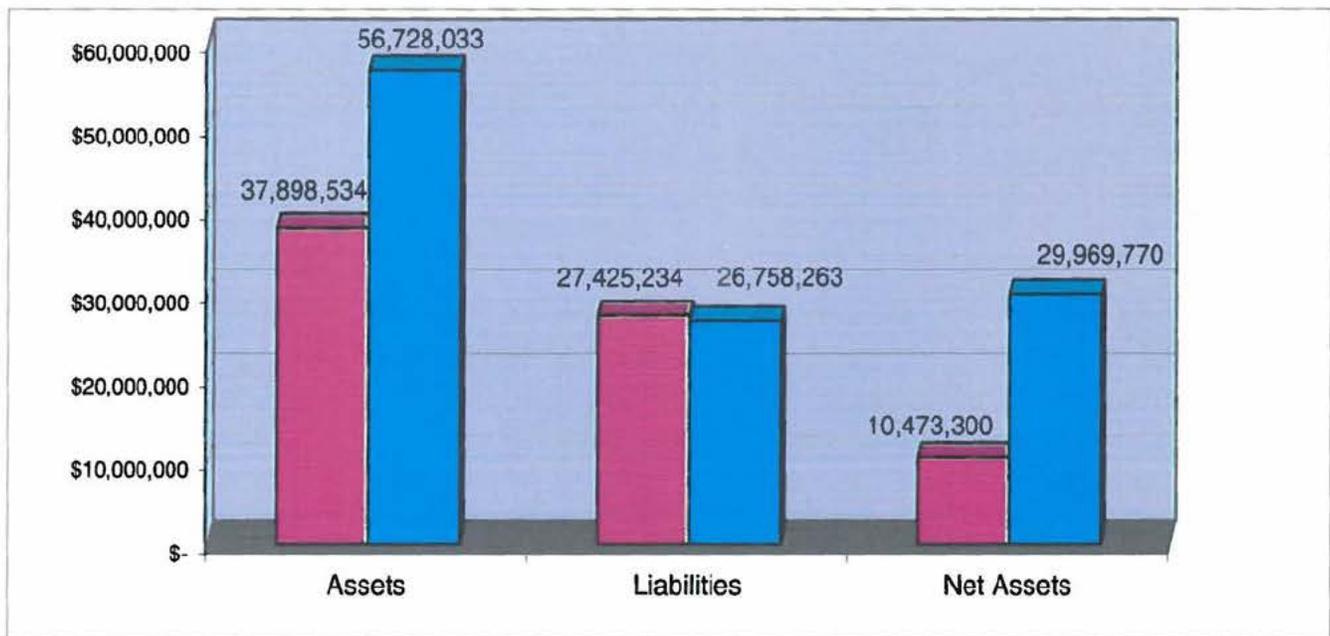
The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Río Grande, primary government assets exceeded total liabilities by \$10,473,300 at the end of 2005, compared to \$29,969,770 at the end of the previous year, as showed in the following condensed Statement of Net Assets of the Primary Government.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

Condensed Statement of Net Assets	2005	2004	Change	%
Current and other assets	\$ 17,435,635	\$ 24,339,761	\$ (6,904,126)	(28%)
Capital assets	20,462,899	32,388,272	(11,925,373)	(37%)
Total assets	37,898,534	56,728,033	(18,829,499)	(33%)
Current and other liabilities	6,184,184	8,536,256	(2,352,072)	(28%)
Long-term liabilities	21,241,050	18,222,007	3,019,043	17%
Total liabilities	27,425,234	26,758,263	666,971	2%
Invested in capital assets, net of related debt	15,775,899	27,400,890	(11,624,991)	(42%)
Restricted	10,494,371	8,683,152	1,811,219	21%
Unrestricted deficit	(15,796,970)	(6,114,272)	(9,682,698)	158%
Total net assets	\$ 10,473,300	\$ 29,969,770	\$ (19,496,470)	(65%)



Changes in Net Assets

The change in net assets is mainly to: (1) the revaluation of the usufruct land owned by the Municipality and (2) the adjustment to property tax receivable.

- (1) As of June 30, 2004, the Municipality valued the usufruct land at market value. However, the usufruct land should have being recognized in books at 1980 values.
- (2) The Municipality recognized all the property tax advances made during the first sixty days for the fiscal year 2004-05 by the CRIM as a receivable. Only ten percent of these collections belonged to prior years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Approximately 62 percent of the Municipality's total revenue came from taxes, while 36 percent resulted from grants and contributions, including federal aid. Charges for Services provided 2 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for general government, health and welfare services, public works, and community development. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

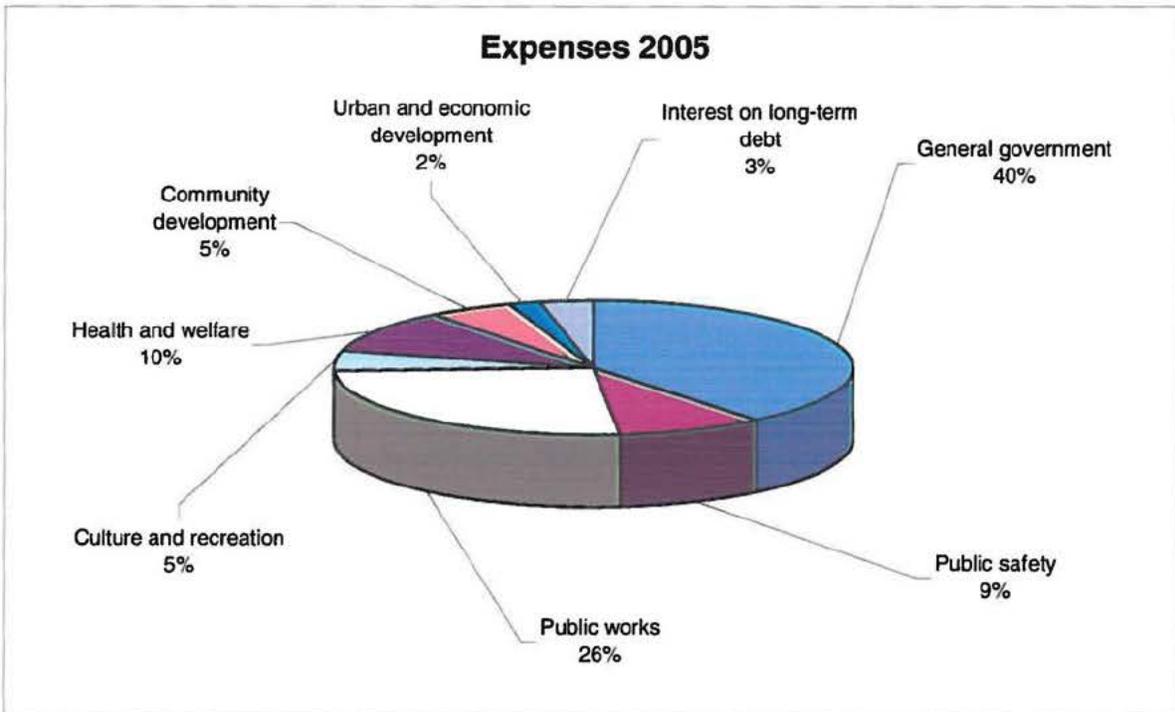
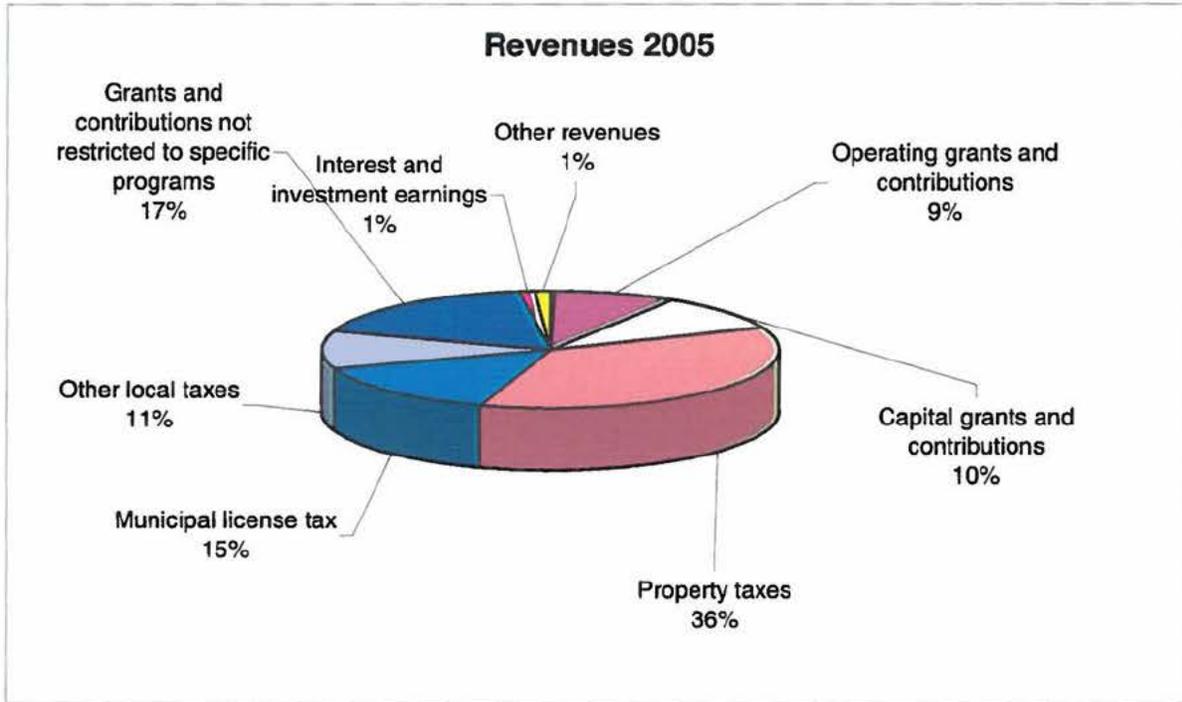
Condensed Statement of Activities	2005	2004	Change	%
Program revenues:				
Charges for services	\$ 63,163	\$ 91,096	\$ (27,933)	(31%)
Operating grants and contributions	1,743,577	1,350,789	392,788	29%
Capital grants and contributions	2,040,093	3,024,699	(984,606)	(33%)
General revenues:				
Property taxes	7,309,588	7,297,629	11,959	-
Municipal license tax	2,959,724	2,346,971	612,753	26%
Other local taxes	2,186,558	3,324,269	(1,137,711)	(34%)
Grants and contributions not restricted to specific programs	3,501,697	3,529,383	(27,686)	(1%)
Interest and investment earnings	271,371	162,408	108,963	67%
Other revenues	204,789	1,413,268	(1,208,479)	(86%)
Total revenues	20,280,560	22,540,512	(2,259,952)	(10%)
Expenses:				
General government	9,563,927	4,642,895	4,921,032	106%
Public safety	2,218,604	3,379,433	(1,160,829)	(34%)
Public works	6,278,998	2,707,279	3,571,719	132%
Culture and recreation	1,268,483		1,268,483	100%
Health and welfare	2,446,071	4,372,696	(1,926,625)	(44%)
Community development	1,336,009		1,336,009	100%
Urban and economic development	449,208	1,691,635	(1,242,427)	(73%)
Interest on long-term debt	816,299	878,211	(61,912)	(7%)
Total expenses	24,377,599	17,672,149	6,705,450	38%
Change in net assets	(4,097,039)	4,868,363	(8,965,402)	(184%)
Net assets, beginning of year, as restated	14,570,339	25,101,407	(10,531,068)	(42%)
Net assets, end of year	\$ 10,473,300	\$ 29,969,770	\$(19,496,470)	(65%)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$12,761,371, a decrease of \$1,690,512 in comparison with the prior year. There are reservations of fund balance amounting to \$11,506,811. This is the fund balance that it is not available for new spending because it has already been committed 1) \$656,160 to liquidate contracts and purchase orders of the prior fiscal year, 2) \$7,471,250 to pay debt service, 3) \$3,155,871 to pay for capital projects, and 4) \$223,530 for other purposes.

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2005, the general fund has an undesignated fund balance of \$1,254,560.

GENERAL FUND BUDGETARY HIGHLIGHTS

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

The actual General Fund budgetary activities resulted in a favorable balance of \$1,075,878, caused mainly due to unexpected variances in revenue collections from miscellaneous sources.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

The Municipality's investment in capital assets as of June 30, 2005, amounts to \$35,420,936, net of accumulated depreciation of \$14,958,037 (including depreciation charges for the year totaled \$750,352), leaving a net book value of \$20,462,899. This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2005, the Municipality has \$1,036,659 of unexpended proceeds mainly from bonds issuances that are committed to future construction activities.

Debt Administration

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available but the revenue also is very predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2005-2006.

FINAL COMMENTS

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

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. Such has been the case of the financial operation corresponding to fiscal year 2005. It further contemplates to maintain or improve its current levels of Net Assets as indicative of a strong financial position which has been identified as one of the main short and long-term objectives of the Municipality.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at P.O. Box 847, Río Grande, PR 00745 or call (787) 887-2370.

**Commonwealth of Puerto Rico
Municipality of Río Grande
Statement of Net Assets
June 30, 2005**

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 7,034,422
Cash with fiscal agent	9,139,993
Accounts receivable:	
Municipal License Tax	4,000
Property tax	785,628
Intergovernmental	436,794
Interest	34,798
Capital assets	
Land, improvements, and construction in progress	7,355,045
Other capital assets, net of depreciation	13,107,854
Total capital assets	<u>20,462,899</u>
Total assets	<u><u>37,898,534</u></u>
Liabilities	
Accounts payable and accrued liabilities	2,098,324
Due to other governmental entities	179,324
Deferred revenues:	
Municipal license tax	1,630,322
Federal grant revenues	715,683
Interest payable	356,280
Noncurrent liabilities:	
Due within one year	1,204,251
Due in more than one year	21,241,050
Total liabilities	<u><u>27,425,234</u></u>
Net Assets	
Invested in capital assets, net of related debt	15,775,899
Restricted for:	
Capital projects	3,155,871
Debt service	7,114,970
Other purposes	223,530
Unrestricted (deficit)	<u>(15,796,970)</u>
Total net assets	<u><u>\$ 10,473,300</u></u>

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

**Commonwealth of Puerto Rico
Municipality of Río Grande
Statement of Activities
For the Year Ended June 30, 2005**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 9,563,927	\$ 11,968	\$ -	\$ 293,516	\$ (9,258,443)
Public safety	2,218,604	21,262	160,216		(2,037,126)
Public works	6,278,998	29,933	72,994	156,302	(6,019,769)
Health and welfare	2,446,071		999,605	10,810	(1,435,656)
Culture and recreation	1,268,483		67,698	237,712	(963,073)
Economic development	260,871		429,956		169,085
Community development	1,336,009			1,341,753	5,744
Urban development	188,337				(188,337)
Education			13,108		13,108
Interest on long-term debt	816,299				(816,299)
Total governmental activities	\$ 24,377,599	\$ 63,163	\$ 1,743,577	\$ 2,040,093	(20,530,766)
General revenues:					
Property taxes					7,309,588
Municipal license tax					2,959,724
Other local taxes					2,186,558
Grants and contributions not restricted to specific programs					3,501,697
Interest and investment earnings					271,371
Miscellaneous					204,789
Total general revenues					16,433,727
Change in net assets					(4,097,039)
Net assets - beginning, as restated					14,570,339
Net assets - ending					\$ 10,473,300

**Commonwealth of Puerto Rico
Municipality of Rio Grande
Balance Sheet
Governmental Funds
June 30, 2005**

	General Fund	Special Revenue Fund Federal Grants	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Assets						
Cash and cash equivalents	\$ 3,686,249	\$ 602,168	\$ 2,275,912	\$ -	\$ 470,093	\$ 7,034,422
Cash with fiscal agent	901,998	398	1,036,659	7,200,938		9,139,993
Accounts receivable:						
Municipal license tax	4,000					4,000
Property Tax	64,964			296,410		361,374
Intergovernmental		373,312			63,482	436,794
Interest	20,700			14,098		34,798
Due from other funds	603,281				30,006	633,287
Total assets	<u>\$ 5,281,192</u>	<u>\$ 975,878</u>	<u>\$ 3,312,571</u>	<u>\$ 7,511,446</u>	<u>\$ 563,581</u>	<u>\$ 17,644,668</u>
Liabilities and Fund Balances						
Liabilities :						
Accounts payable and accrued liabilities	\$ 1,535,387	\$ 32,594	\$ 156,700	\$ -	\$ -	\$ 1,724,681
Due to other governmental entities	179,324					179,324
Due to other funds		477,334		40,196	115,757	633,287
Deferred revenues:						
Municipal license tax	1,630,322					1,630,322
Federal grant revenues		465,950			249,733	715,683
Total liabilities	<u>3,345,033</u>	<u>975,878</u>	<u>156,700</u>	<u>40,196</u>	<u>365,490</u>	<u>4,883,297</u>
Fund balances:						
Reserved for:						
Encumbrances	656,160					656,160
Capital projects			3,155,871			3,155,871
Debt service fund				7,471,250		7,471,250
Other purposes	25,439					25,439
Reserved reported in nonmajor funds:						
Other purposes					198,091	198,091
Unreserved:						
Undesigned	1,254,560					1,254,560
Total fund balances	<u>1,936,159</u>		<u>3,155,871</u>	<u>7,471,250</u>	<u>198,091</u>	<u>12,761,371</u>
Total liabilities and fund balances	<u>\$ 5,281,192</u>	<u>\$ 975,878</u>	<u>\$ 3,312,571</u>	<u>\$ 7,511,446</u>	<u>\$ 563,581</u>	
Amounts reported for governmental activities in the statement of net assets are different because:						
Accrual basis of accounting accounts receivable recognized in government-wide financial statements						424,254
Accrual basis of accounting accounts payable recognized in government-wide financial statements						(373,643)
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds						20,462,899
Long-term liabilities, including accrued interest payable, are not due and payable in the current period, and therefore, are not reported in the funds						(22,801,581)
Net assets of governmental activities						<u>\$ 10,473,300</u>

Commonwealth of Puerto Rico
Municipality of Rio Grande
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2005

	General Fund	Special Revenue Fund Federal Grants	Capital Project Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Revenues						
Property taxes	\$ 5,665,999	\$ -	\$ -	\$ 1,682,792	\$ -	\$ 7,348,791
Municipal license taxes	2,887,594				72,130	2,959,724
Licenses, permits and other local taxes	2,198,526					2,198,526
Intergovernmental	3,501,697		404,824		684,716	4,591,237
Fines and forfeitures	21,262					21,262
Rent of property	29,933					29,933
Interest	271,371					271,371
Federal grants		1,787,916			471,044	2,258,960
Miscellaneous	180,395	1,551	7,226		157,271	346,443
Total revenues	14,756,777	1,789,467	412,050	1,682,792	1,385,161	20,026,247
Expenditures						
Current:						
General government	6,550,252		3,673		50,844	6,604,769
Public safety	2,064,497	34			136,251	2,200,782
Public works	5,533,708	39,433	236,486		430,948	6,240,575
Health and welfare	1,370,467	389,967	41,612		619,131	2,421,177
Culture and recreation	645,186	20,768	329,557		14,750	1,010,261
Economic development					260,871	260,871
Community development		1,341,753				1,341,753
Urban development			188,337			188,337
Debt service:						
Principal				651,000		651,000
Interest				826,740		826,740
Total expenditures	16,164,110	1,791,955	799,665	1,477,740	1,512,795	21,746,265
Excess (deficiency) of revenues over (under) expenditures	(1,407,333)	(2,488)	(387,615)	205,052	(127,634)	(1,720,018)
Other financing sources (uses)						
Transfers in			1,277,451	81,750	144,655	1,503,856
Transfers out	(1,107,837)	(174,539)	(47,630)		(173,850)	(1,503,856)
Total other financing sources (uses)	(1,107,837)	(174,539)	1,229,821	81,750	(29,195)	-
Net change in fund balances	(2,515,170)	(177,027)	842,206	286,802	(156,829)	(1,720,018)
Fund balance, beginning as restated	4,451,329	177,027	2,313,665	7,184,448	354,920	14,481,389
Fund balance, ending	<u>\$ 1,936,159</u>	<u>\$ -</u>	<u>\$ 3,155,871</u>	<u>\$ 7,471,250</u>	<u>\$ 198,091</u>	<u>\$ 12,761,371</u>

**Commonwealth of Puerto Rico
Municipality of Río Grande
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2005**

Net Change in Fund Balances - Total Governmental Funds **\$ (1,720,018)**

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

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period. 1,140,443

Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Change in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds. (750,353)

Interest expense on long-term debt was reported in the Government-Wide Statement of Activities and Change in Net Assets, but it did not require the use of current financial resources. Therefore, interest expense was not reported as expenditures in Governmental Funds. The following amount represented the change in accrued interest from prior year. 10,441

Bonds and notes proceeds provides current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide Statement of Net Assets. Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long-term liabilities in the Government-Wide Statement of Net Assets. This is the amount paid in the current year. 651,000

Repayment of long term Treasury Department debt is an expenditure in Governmental Funds, but the repayment reduces long-term debt in the Government-Wide Statement of Net Assets. This is the amount paid in the current year. 27,015

Repayment of long term property tax advance debt is an expenditure in Governmental Funds, but the repayment reduces long-term property tax advance debt in the Government-Wide Statement of Net Assets. The following amount represent the change in long-term property tax advance debt from prior year. (2,203,454)

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenue in the funds. The following amount represents the change in this revenues from prior year. (39,203)

Some expenses reported in the Governmental Funds do not require the use of current financial resources and, therefore, are not reported as expenses in the Statement of Activities. The following amount represents the change in this expenses from prior year. (37,157)

Long-term federal cost disallowances are reported in the Governmental-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, federal cost disallowances are not reported as expenditures in Government Funds. The following amount represent the change in long-term federal cost disallowances from prior year. (49,385)

Long-term claims and judgements are reported in the Governmental-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, claims and judgments are not reported as expenditures in Government Funds. The following amount represent the change in long-term claims and judgments from prior year. (1,184,338)

Account payables reported in the Government-Wide Statement of Activities and Change in Net Assets but not reported as in the Governmental Funds because they do not require the use of current financial resources. This is the amount reported in the current period. (373,643)

Long-term compensated absences are reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represent the change in long-term compensated absences from prior year. 431,613

Change in Net Assets of Governmental Activities **\$ (4,097,039)**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2005

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Río Grande** (the Municipality) was founded on the year 1840. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a sixteen member Municipal Legislature who are elected for a four-year term.

The Municipality provides a full range of services for its citizens. These services include public safety, public works, culture and recreation, health and welfare, community development, education, and other miscellaneous services.

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

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's and Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. The Statement was adopted as of July 1, 2002. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

As part of this Statement, there is a new reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). This requirement permits an optional four-year delay for implementation to fiscal year ended on June 30, 2007. The Municipality has elected to delay the capitalization of infrastructure.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

A. Component Units

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, The Financial Reporting Entity, of the GASB, as amended by GASB Statement No. 39. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

B. Government-wide and fund financial statements

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

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

Special Revenue Fund - Federal Grants- is the accounting entity in which revenues derived from federal grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal statutes.

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

C. Financial reporting presentation

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

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

Special Revenue Fund - Local and State Grants - Special Revenue Funds are used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Section 8 - Special Revenue Funds are used to account for revenues derived from section 8 choice voucher program. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Federal Grants - Special Revenue Funds are used to account for revenues derived from federal grants. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Projects Fund - State and Local Grants - Capital Projects Fund are used to account for financial resources used for the acquisition or construction of major capital facilities.

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

D. Measurement focus, basis of accounting and financial presentation

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

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

Property taxes, franchise taxes, licenses, rent, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

Private-sector standards of accounting and financial reporting issue prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

E. Assets, liabilities and net assets

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

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

- 2. Receivables and payables-** Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivable in the special revenue or capital project funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded or state funded programs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

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

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

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Buildings and site improvements	30 to 50 years	\$1
Infrastructure	20 to 50 years	\$1
Works of art	10 years	\$1
Vehicles	8 years	\$1
Furniture and fixtures	5 to 20 years	\$25
Machinery and equipment	5 to 20 years	\$25

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

7. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.
8. **Reservation of fund balance-** Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:
- a. **Capital Projects-** Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
 - b. **Encumbrances-** Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
 - c. **Other Purposes-** Represents net assets available for specific use and/or legally segregated for other specific future use.
 - d. **Debt Service Fund-** Represents net assets available to finance future debt service payments.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

9. Interfund and intra-entity transactions- The Municipality has the following types of transactions among funds:

- a. **Operating Transfers-** Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
- b. **Intra-Entity Transactions-** Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.

10. Risk financing- The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2005 amounted to approximately \$139,763. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$300,272 for workers compensation insurance covering all municipal employees.

11. Reconciliation of Government-wide and Fund Financial Statements

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

The details of this reconciliation are as follows:

		<u>Total Net Assets</u> <u>Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 20,462,899	
Deduct:		
Bonds and notes payable	<u>(4,687,000)</u>	\$ 15,775,899
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		3,155,871
<u>Net assets restricted for debt service</u>		
Fund balance restricted for debt service	7,471,250	
Deduct:		
Interest Payable	(356,280)	7,114,970
<u>Net assets restricted for other purposes</u>		
Other governmental funds—fund balance restricted for other purposes		198,091
<u>Net assets unrestricted (deficit)</u>		
General fund – total fund balance:	\$ 1,936,159	
Add:		
Accrual basis accounts receivable	424,254	
Deduct:		
Accrual basis accounts payable	(373,643)	
Bonds Payable	(11,249,000)	
Property Tax-Treasury	(193,722)	
Property Tax-Advance	(517,214)	
CRIM-Law 146	(1,686,241)	
Compensated absences	(1,830,789)	
Claims and judgments	(1,509,068)	
Reserve for federal cost disallowances	<u>(772,267)</u>	<u>(15,771,531)</u>
Total net assets – governmental activities		<u>\$ 10,473,300</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

2. DEPOSITS

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

The Municipality's bank balances in commercial banks of \$3,686,249 in the general fund, \$602,168 in the special revenue fund – federal grants, and \$2,275,912 in the capital projects fund – state and local grants were fully collateralized at June 30, 2005. In the other governmental funds there were deposits with commercial banks of \$470,093 that were fully collateralized.

The deposits at GDB of \$901,998 in the general fund, the \$398 in the special revenue fund – federal grants, the \$1,036,659 in the capital projects fund – state and local grants, and the \$7,200,938 that is restricted for debt service fund, are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

A. *Municipal License Tax*- The Municipality impose a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2005, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues

2. Other organizations- 0.50% of gross revenues

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2005, net of allowance for uncollectible.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

3. RECEIVABLES (CONTINUED)

B. *Intergovernmental Receivables*- Intergovernmental receivable in special revenue fund – federal grants represent expenditures incurred not yet reimbursed by the federal government. Following is a detail of the intergovernmental receivable:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grant – Entitlement Grant	\$ 111,313
Child Care and Development Block Grant	174,550
Community Service Block Grant	<u>87,449</u>
Total	<u>\$ 373,312</u>

Intergovernmental receivable in the debt service fund represents the amounts due from the CRIM resulting from the excess of current year property tax collections over current year advances. Following is a detail of the intergovernmental receivables:

<u>Governmental Entity</u>	<u>Amount</u>
Municipal Revenue Collection Center (CRIM)	<u>\$ 296,410</u>
Total	<u>\$ 296,410</u>

Intergovernmental receivable in the other governmental funds represent expenditures incurred not yet reimbursed by other governmental entities. Following is a detail of the intergovernmental receivable:

<u>Program Description</u>	<u>Amount</u>
Commonwealth of Puerto Rico-Department of Labor and Human Resources– Law 52 Grant	<u>\$ 63,482</u>
Total	<u>\$ 63,482</u>

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2005, and interfund transfers during the fiscal year ended at June 30, 2005, are summarized as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

4. INTERFUND TRANSACTIONS (CONTINUED)

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund - Federal Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	\$ 447,328
General Fund	Debt Service Fund	Interest Revenue	40,196
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	115,757
Other Governmental Funds	Special Revenue Fund - Federal Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	<u>30,006</u>
Total			<u>\$ 633,287</u>

b. Transfer in/out to other fund

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	\$ 881,432
General Fund	Debt Service Fund	Debt retirement	81,750
General Fund	Other Governmental Funds	Transfer of funds to Other Governmental Funds	144,655
Special Revenue Fund - Federal Grants	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	174,539
Capital Projects Fund - State and Local Grants	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	47,630
Other Governmental Funds	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	<u>173,850</u>
Total			<u>\$ 1,503,856</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

5. CAPITAL ASSETS

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2005, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

<u>Governmental Activities:</u>	<u>Balance</u> <u>July 1, 2004</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance</u> <u>June 30, 2005</u>
Capital asset, not being depreciated:				
Land	\$ 1,194,589	522		1,195,111
Construction in progress	<u>5,704,402</u>	<u>455,531</u>	-	<u>6,159,933</u>
Total capital assets not being depreciated	<u>6,898,991</u>	<u>456,053</u>	-	<u>7,355,044</u>
Capital assets, being depreciated:				
Buildings and building improvements	15,041,086	3,950		15,045,036
Infrastructure	1,907,946	293,516		2,201,462
Infrastructure improvements	4,624,953			4,624,953
Equipment	1,531,598	187,639		1,719,237
Furnishing		35,413		35,413
Computers		8,178		8,178
Vehicles	<u>4,275,919</u>	<u>155,694</u>	-	<u>4,431,613</u>
Total capital assets being depreciated	<u>27,381,502</u>	<u>684,390</u>	-	<u>28,065,892</u>
Less accumulated depreciation for:				
Buildings and building improvements	(5,002,378)	(303,121)		(5,305,499)
Infrastructure	(558,427)	(74,523)		(632,950)
Infrastructure improvements	(4,597,570)	(5,868)		(4,603,438)
Equipment	(792,941)	(108,924)		(901,865)
Furnishing		(1,249)		(1,249)
Computers		(50)		(50)
Vehicles	<u>3,256,369</u>	<u>(256,617)</u>	-	<u>(3,512,986)</u>
Total accumulated depreciation	<u>14,207,685</u>	<u>(750,352)</u>	-	<u>(14,958,037)</u>
Total capital assets being depreciated, net	<u>13,173,817</u>	<u>(65,962)</u>	-	<u>13,107,855</u>
Governmental activities capital assets, net	<u>\$ 20,072,808</u>	<u>390,091</u>	-	<u>20,462,899</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

5. CAPITAL ASSETS (CONTINUED)

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

Governmental activities:

General government	\$ 70,740
Public safety	129,711
Public works	253,164
Culture and recreation	271,843
Health and welfare	<u>24,894</u>
Total depreciation expense-governmental activities	<u>\$ 750,352</u>

6. PROPERTY TAXES

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

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the final liquidation noting that the advances exceeded collections by \$208,230. This excess will not be funded with available expendable financial resources at June 30, 2005. Based on this, such amount was presented in the government-wide financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

6. PROPERTY TAXES (CONTINUED)

The Municipality entered into an agreement with the Commonwealth of Puerto Rico for the repayment of excess property tax advances. As of June 30, 2005, the related unpaid property tax advances presented in the statement of net assets amounted to approximately \$193,722.

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

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

On June 26 1997, Public Law Num. 21 was enacted authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable o equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities thru a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law. As of June 30 2005, the related unpaid property tax advances presented in the Statement of Net Assets amounted to approximately \$1,686,241.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

6. PROPERTY TAXES (CONTINUED)

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

The annual tax rate is 8.23% for real property and 6.23% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.40% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

7. DUE TO OTHER GOVERNMENTAL ENTITIES:

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

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Telephone Company	\$ 91,165
Puerto Rico Aqueduct and Sewer Authority	48,126
General Services Administration	22,121
Department of Labor and Human Resources	<u>17,912</u>
Total	<u>\$ 179,324</u>

8. DEFERRED REVENUES

- A. Municipal License Tax-** The deferred revenues of approximately \$1,630,322 in the general fund relates to municipal license tax collected in fiscal year 2004-05 that will be earned in fiscal year 2005-06.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

8. DEFERRED REVENUES (CONTINUED)

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

<u>Program Description</u>	<u>Amount</u>
Section 8 Housing Choice Voucher	\$ 249,733
Wildlife Restoration	38,736
Housing Opportunities for Persons with AIDS	48,150
Public Assistance Grant	331,297
Urban Development Action Grant	14,368
Grants for Supportive Services and Senior Centers	12,036
Community Development Block Grant	9,254
Others	<u>12,109</u>
Total	<u>\$ 715,683</u>

9. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2005, was as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds Payable	\$ 16,587,000	\$ -	\$ (651,000)	\$15,936,000	\$ 579,000
Property Tax-Treasury	220,737		(27,015)	193,722	28,397
Property Tax-Advance		517,214		517,214	308,984
CRIM - Law 146		1,686,241		1,686,241	
Compensated absences	2,262,402		(431,613)	1,830,789	94,803
Claims and Assessments	324,731	1,451,504	(267,167)	1,509,068	
Reserve for federal cost disallowances	722,882	165,154	(115,769)	772,267	193,067
Obligation under capital leases	<u>7,879</u>	<u>-</u>	<u>(7,879)</u>	<u>-</u>	<u>-</u>
Total	<u>\$20,125,631</u>	<u>\$3,820,113</u>	<u>\$(1,500,443)</u>	<u>\$22,445,301</u>	<u>\$1,204,251</u>

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

9. LONG-TERM LIABILITIES (CONTINUED)

2. Bonds payable- The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. Bonds payable outstanding at June 30, 2005 are as follows:

<u>Type of bonds</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest Rates</u>	<u>Balance at June 30, 2005</u>
1991-Series	7/1/2005	\$ 155,000	6.26%	\$ 20,000
1995-Series	1/1/2019	1,187,000	4.50%	897,000
1996-Series	7/1/2020	1,045,000	5.93% to 6.63%	865,000
1996-Series	7/1/2020	1,715,000	5.93% to 6.63%	1,430,000
1998-Series	7/1/2012	355,000	5.42% to 6.04%	240,000
2002-Series	7/1/2026	5,105,000	5.00% to 8.00%	4,885,000
2002-Series	7/1/2016	1,400,000	2.89% to 4.91%	1,235,000
2002-Series	7/1/2008	1,055,000	2.89% to 3.88%	675,000
2003-Series	7/1/2027	4,746,000	6.50%	4,579,000
2003-Series	7/1/2027	1,175,000	6.50%	<u>1,110,000</u>
Total general obligation bonds				<u>\$15,936,000</u>

These bonds, except the 2003 Series \$1,175,000 bond, are payable from the ad valorem property tax of 1.40% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes. The 2003 Series \$1,175,000 bond is payable with General Fund resources.

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

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 579,000	\$ 805,723
2007	597,000	997,157
2008	647,000	964,375
2009	696,000	928,154
2010	547,000	892,269
2011-2015	3,299,000	3,885,710
2016-2020	3,942,000	2,699,349
2021-2025	3,563,000	1,392,943
2026-2030	<u>2,066,000</u>	<u>192,488</u>
Total	<u>\$ 15,936,000</u>	<u>\$ 12,758,168</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

9. LONG-TERM LIABILITIES (CONTINUED)

- 3. Compensated absences-** The government-wide statement of net assets includes approximately \$979,019 of accrued sick leave benefits, and approximately \$851,770 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.
- 4. Federal cost disallowances-** At June 30, 2005, the accompanying statement of net assets presents a reserve for ineligible and unsupported costs under federally assisted programs amounting to \$772,267.

10. PENSION PLAN

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

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

10. PENSION PLAN (CONTINUED)

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$ 550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions during the year ended June 30, 2005 amounted to approximately \$561,185.

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

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2005, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940.

11. RISK MANAGEMENT

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

12. CAPITAL ASSETS REPORTED VALUE

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

13. CONTINGENCIES

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities.

With respect to pending and threatened litigation, the Municipality has reported liabilities of approximately \$1,509,068 for awarded and anticipated unfavorable judgments. This amount was included in the financial statements and represents the amount estimated as probable liability or a liability with a fixed or expected due date, which will require future available financial resources for its payment.

It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

14. BEGINNING FUND BALANCES RESTATEMENT

The following restatements have been made in the financial statements, which are reported as an adjustment to beginning fund balance or net assets:

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

14. BEGINNING FUND BALANCES RESTATEMENT (CONTINUED)

**Adjustments to fund balance of governmental funds in the
fund financial statements:**

General Fund

Corrections to the property tax receivable	\$ (991,448)
Reclassification of funds from General Fund to Special Revenue and Capital Projects Funds, to conform with the Current Basic Financial Statements presentation	(1,100,449)
Accrued liabilities not previously recorded	(270,690)
Others adjustments	<u>(41,051)</u>
Total decrease in fund balance	<u>(2,403,638)</u>

Special Revenue Fund - Federal Grants

Deferred revenue not previously recorded	<u>140,779</u>
Total increase in fund balance	<u>140,779</u>

Capital Projects Fund - State & Local Grants

Reclassification of funds from General Fund to Capital Projects Funds, to conform with the Current Basic Financial Statements presentation	493,136
Revenue earned recorded as deferred	477,438
Reclassification of special revenue fund - federal grant classified in capital projects fund in the previous year	194,098
Others adjustments	<u>(9,070)</u>
Total increase in fund balance	<u>1,155,602</u>

Debt Service Fund

Corrections to the property tax receivable	(193,192)
Reclassification of accounts payable	837,259
Accrued revenue not previously recorded	<u>91,797</u>
Total increase in fund balance	<u>735,864</u>

Other Governmental Funds

Reclassification of funds from General Fund to Special Revenue Funds, to conform with the Current Basic Financial Statements presentation	607,312
Reclassification of deferred recognized as revenue	(252,285)
Others adjustments	<u>45,872</u>
Total increase in fund balance	<u>400,899</u>

Net increase in fund balance, governmental funds **\$ 29,506**

**Adjustments to net assets in the government-wide financial
statement**

Corrections to the property tax receivable	\$ (3,628,215)
Change in land reported value	(12,285,721)
Others adjustments	<u>514,505</u>

Total decrease in net assets **\$(15,399,431)**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

**BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
(SEE NOTES TO BUDGETARY COMPARISON SCHEDULE)**

YEAR ENDED JUNE 30, 2005

	<u>Budgeted Amounts</u>		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 5,595,337	\$ 5,595,337	\$ 5,672,199	\$ 76,862
Fines and forfeiture	3,000	3,000	21,262	18,262
Municipal license tax	2,251,500	2,251,500	2,913,593	662,093
Licenses, permits and other local taxes	3,315,000	3,315,000	2,198,526	(1,116,474)
Intergovernmental	3,508,831	3,508,831	3,501,697	(7,134)
Interest	175,000	175,000	231,445	56,445
Rent of property	30,000	30,000	29,933	(67)
Miscellaneous	<u>235,000</u>	<u>235,000</u>	<u>180,395</u>	<u>(54,605)</u>
Total revenues	<u>15,113,668</u>	<u>15,113,668</u>	<u>14,749,050</u>	<u>(364,618)</u>
Budget carryover (1)		2,919,244	2,919,244	
Total revenues after carryover	<u>15,113,668</u>	<u>18,032,912</u>	<u>17,668,294</u>	<u>(364,618)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
General government	4,972,926	6,094,482	5,664,043	430,439
Public safety	2,382,442	2,455,060	2,084,933	370,127
Public works	5,574,962	6,296,672	5,794,128	502,544
Health and welfare	1,430,940	1,441,822	1,375,806	66,016
Culture and recreation	653,623	846,101	791,756	54,345
Operating transfer to other funds	<u>98,775</u>	<u>898,775</u>	<u>881,750</u>	<u>17,025</u>
Total expenditures, encumbrances and other financing uses	<u>15,113,668</u>	<u>18,032,912</u>	<u>16,592,416</u>	<u>1,440,496</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,075,878</u>	<u>\$ 1,075,878</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 17,668,294
Differences-budget to GAAP:				
Budget Carryover				(2,919,244)
GAAP adjustments to revenues				<u>7,727</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 14,756,777</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 16,592,416
Differences-budget to GAAP:				
Non-budgeted expenditures				212,129
Prior year encumbrances recorded as current year expenditures for GAAP basis				897,475
Current year encumbrances recorded as expenditures for budgetary purposes				(656,160)
No budgeted transfer out				<u>226,087</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 17,271,947</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

NOTES TO BUDGETARY COMPARISON SCHEDULE – GENERAL FUND

YEAR ENDED JUNE 30, 2005

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

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

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2005 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2005.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2005

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Community Development Block Grants/Entitlement Grants	14.218		1,341,752
Direct Program:			
Section 8 Housing Choice Vouchers	14.871		471,044
Pass-through the Commonwealth of Puerto Rico - Municipality of San Juan:			
Housing Opportunities for Persons with Aids	14.241	Not Available	<u>111,641</u>
Total U.S. Department of Housing and Urban Development			<u>1,924,437</u>
U.S. DEPARTMENT OF THE INTERIOR			
Direct Program:			
Wildlife Restoration	15.611	Not Available	<u>20,768</u>
Total U.S. Department of the Interior			<u>20,768</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

YEAR ENDED JUNE 30, 2005

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES:			
Pass-through the Commonwealth of Puerto Rico – Governor's Office (Elderly Office):			
Special Program for Aging – Title III, Part B – Grant for Supporting Services and Senior Centers	93.044	Not Available	50,654
Community Services Block Grant	93.569	Not Available	65,544
Child Care and Development Block Grant	93.575	Not Available	<u>160,650</u>
Total U.S. Department of Health and Human Services			<u>276,848</u>
U.S. DEPARTMENT OF HOMELAND SECURITY			
Pass-through the Commonwealth of Puerto Rico Governor Authorized Representative (GAR):			
Public Assistance Grants	83.544	Not Available	<u>30,425</u>
Total U.S. Department of Homeland Security			<u>30,425</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 2,252,478</u>

The accompanying notes are an integral part of this schedule

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2005

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the **Municipality of Río Grande** and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the fund financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Other Governmental Funds in the Municipality's fund financial statements. The reconciliation between the expenditures in the funds financial statements and the disbursements in the Schedule of Expenditures of Federal Awards is as follows:

Description	Special Revenue Fund -Other Federal Grants	Other Governmental Funds	Total
Per Schedule of Expenditures of Federal Awards	\$ 1,781,434	\$ 471,044	\$ 2,252,478
Non federal programs expenditures	10,521	1,041,751	1,052,272
Total expenditures in the general purpose financial Statements	<u>\$ 1,791,955</u>	<u>\$ 1,512,795</u>	<u>\$ 3,304,750</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Río Grande
Río Grande, Puerto Rico**

We have audited the basic financial statements of the **Municipality of Río Grande** as of and for the year ended June 30, 2005, and have issued our report thereon dated December 21, 2005, which was unqualified at the fund financial statements level, but adverse at the government-wide financial statements level because we were unable to obtain competent evidential matter related to the Capital Assets reported in the governmental activities. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the **Municipality of Río Grande's** basic 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 basic financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Río Grande's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting that, in our judgment, could adversely affect **Municipality of Río Grande's** ability to record, process, summarize, and report financial data consistent with the assertions of management in the basic financial statements. The reportable conditions are described in the accompanying schedule of findings and questioned costs as items **05-01** and **05-02**.

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS (CONTINUED)

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 general purpose 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 reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management of the Municipality of Río Grande in a separate letter dated December 21, 2005.

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

Lopez Vega CPA, PSC
LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 21, 2005

Stamp No. 2106104 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.





López-Vega, CPA, PSC

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

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Río Grande
Río Grande, Puerto Rico**

Compliance

We have audited the compliance of the **Municipality of Río Grande** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2005. The **Municipality of Río Grande's** major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the **Municipality of Río Grande's** management. Our responsibility is to express an opinion on the **Municipality of Río Grande'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 the *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **Municipality of Río Grande's** compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the **Municipality of Río Grande's** compliance with those requirements.

In our opinion, the **Municipality of Río Grande** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2005. 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, **05-03 through 05-08**.

**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133
(CONTINUED)**

Internal Control Over Compliance

The management of the **Municipality of Río Grande** 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 Río Grande's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the **Municipality of Río Grande'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 **05-03** through **05-08**.

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 on 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 material weakness. However, of the reportable conditions described above, we consider items **05-03** and **05-08**, to be material weaknesses. We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Río Grande** in a separate letter dated February 17, 2006.



INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133
(CONTINUED)

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.


LÓPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
February 17, 2006

Stamp No. 2106105 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2005

Section I – Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unqualified	
Internal control over financial reporting:		
Material weakness identified?	Yes	No <input checked="" type="checkbox"/>
Reportable conditions identified not considered to be material weaknesses?	Yes <input checked="" type="checkbox"/>	None reported
Noncompliance material to financial statements noted?	Yes	No <input checked="" type="checkbox"/>

Federal awards

Internal Control over major programs:		
Material weakness identified?	Yes <input checked="" type="checkbox"/>	No
Reportable conditions identified not considered to be material weaknesses?	Yes <input checked="" type="checkbox"/>	None reported

<u>Type of auditor's report issued on compliance for major programs:</u>	Unqualified
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Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes <input checked="" type="checkbox"/>	No
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Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
14.218	Community Development Block Grant - Entitlement Grant
14.871	Section 8 Housing Choice Voucher
Dollar threshold used to distinguish between Type A and Type B programs	\$ 300,000
Auditee qualified as low-risk auditee?	Yes <input type="checkbox"/> No <input checked="" type="checkbox"/>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section II – Financial Statements Findings

Finding Reference	05-01
Requirement	Cash Receipts – Revenue, Receivable - Collections
Statement of Condition	<p>We performed a cash receipt test and examined a sample of twenty-five (25) collections. The following summarize the exceptions found:</p> <ul style="list-style-type: none">a. In one (1) case by the amount of \$21,717.74, the file do not include the Municipal License Tax Certificate nor the Income Tax Return or Audited Financial Statements. As a result, we can't determine the taxpayer obligation.
Criteria	<p>The Chapter (9) of the Revised Regulation on Basic Standards for Municipalities of Puerto Rico state that the Municipality should maintain adequately documented taxpayers files, including a set of financial statements for taxpayers with a volume of business in excess of one million dollars, municipal license taxes certificate, income tax return, etc.</p>
Cause of Condition	<p>The internal control procedures fail to assure that taxpayer files are properly documented and daily collections are duly accounted.</p>
Effect of Condition	<p>In these cases the Municipality did not comply with regulations stated in The Section Four (4) of the Chapter three (3) and Chapter nine (9) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.</p>
Questioned Costs	<p>None</p>
Recommendation	<p>Municipality should implement the following procedures in order to avoid these situations in a future:</p> <ul style="list-style-type: none">a. Establish procedures to assure that excise tax files include evidence of Construction permits.b. Assign an employee to review that all Municipal License Tax taxpayers who requested a time extension in order to ascertain that they submitted the audited financial statement as required by law. In case of noncompliance with the time extension the Municipality should proceed to eliminate the 5% discount taken and apply interest and penalties.c. Assign an employee to revise all sales volume taxpayers' files to verify if such files include all documents required by law.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section II – Financial Statements Findings

Finding Reference 05-01 (Continued)

Requirement **Cash Receipts – Revenue, Receivable - Collections**

Management Response

And Corrective Action The Municipality Management instructed Treasury Department staff to assure that all taxpayer's files include all required documentation; primarily, Municipal License Tax Certificate and Income Tax Return or Audited Financial Statements.

Implementation Date: April 2006

Responsible Person: Mr. Isaías Rivera Estrella
Finance Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section II – Financial Statements Findings

Finding Reference	05-02
Requirement	Expenditures for Goods and Services and Accounts Payables- Purchasing and receiving
Statement of Condition	<p>We performed a cash disbursement test and examined fourteen (14) disbursement vouchers which belonged to CDBG Program, and forty six (46) disbursement vouchers which belonged to the General Fund and Local and State Fund. The following summarize the internal control exceptions noted:</p> <ul style="list-style-type: none">a. In one (1) case for the amount of approximately \$741.26, the Purchase Order was issued after receiving the goods or services.b. In one (1) case the original invoice for the amount of \$3,771.16 was not available for examination. Only a copy was available.c. One (1) disbursement voucher for the amount of \$77,049.50 did not include any documentation detailing the date and signature of the person who received the goods or services in conformity with the Purchase Order (Receiving Report).
Criteria	<p>The Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establish in the Chapter Four (4) that the Finance Director will be responsible to account and prepare disbursements through documents duly prepared and certified.</p>
Cause of Condition	<p>The Municipality internal control failed to assure that all documents supporting disbursement of funds are approved before disbursement of funds.</p>
Effect of Condition	<p>The Municipality is not in compliance with Chapter Four (4) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico.</p>
Recommendation	<p>We recommend that the Municipality should improve its internal control and procedures in order to assure that disbursement vouchers, cancelled checks and other supporting documents are available for examination by auditors and includes all required documentation and approvals.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section II - Financial Statements Findings

Finding Reference 05-02 (Continued)

Questioned Costs None

Management Response

And Corrective Action The Municipal Management instructed Finance Department staff on the following:

- Not receiving goods or services before issuing a purchase order.
- Also, not paying any disbursement voucher that does not contain the original supplier invoice.
- In addition, the Municipal Management gave instructions to pre-interventor to verify that disbursement vouchers include the date and signature of the functionary who received the goods or services in conformity with the purchase order (receiving report).

Implementation Date: April 2006

Responsible Person: Mr. Isaías Rivera Estrella
Finance Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	05-03
Program	Community Development Block Grant/Entitlement Grants (CFDA 14.218); U.S. Department of Housing and Urban Development
Requirement	Davis Bacon Act
Statement of Condition	<p>During our Davis-Bacon Act test for two (2) construction projects, we noted the following situations:</p> <p>a. In the project contract 2004-000217 with a cost of \$121,325, we found no evidence supporting that the federal program staff, applied adequately the monitoring system developed to ensure contractors compliance with payment of prevailing wages rates to employees. Also, we did not find in the contractor's file the contract weekly payrolls related to the period from October, 2004 to December, 2004.</p>
Criteria	Davis-Bacon Act, as amended, DOL (40 USC 276a - 276a-7).
Cause of Condition	The Municipality's internal controls failed to apply all monitoring system procedures developed to test applicable contractors with respect to payment of prevailing wages.
Effect of Condition	The Municipality is not in compliance with Davis-Bacon Act, as amended, DOL (40 USC 276a -276a-7).
Recommendation	We recommend management to follow monitoring system procedures developed, including obtaining contractor's and subcontractor's weekly payrolls to be reviewed on a weekly basis by the responsible municipal employee, and interview contractor's and subcontractor's laborers periodically (up to ten percent (10%) of the workers on long term projects) to establish the degree of compliance and the nature and extent of violations, if any, and then communicate promptly to the contractors any failure in the payroll process.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 05-03 (continued)

Questioned Costs None

**Management Response
and Corrective Action** The Municipality has taken internal controls in order to comply with Davis-Bacon Act. The Department of External Resources has in their staff a Projects Coordinator that personally visits weekly all construction projects and conducts the laborers interview periodically. We're also reviewing the payroll in order to make sure that they're in compliance with the prevailing federal and state's wages rates.

Responsible Person: Mrs. Wanda I. Del Valle-Federal Programs Director

Implementation Date: July 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Mayor Federal Program Award Findings and Questioned Costs

Finding Reference	05-04
Program	Community Development Block Grant/Entitlement Grants (CFDA 14.218); U.S. Department of Housing and Urban Development
Requirement	Financial Reporting
Statement of Condition	During our audit of Community Development Block Grant- Entitlement Grant we found that the Federal Cash Transaction Report (SF-272) for the period ended 6/30/05 did not trace to the accounting records.
Criteria	OMB Common Rules, Subpart C, Section 85.20 (b) (1), states that the grantee must maintain internal control procedures that permits proper tracing of fund to accounting records. Also, it requires accurate, current and complete disclosure of financial results.
Cause of Condition	The Municipality has not established adequate internal control procedures to assure the correctness of the reports submitted to HUD.
Effect of Condition	The Municipality did not comply with 24 CFR Section 85.20 (b) (1).
Recommendation	We recommend that the Municipality should establish internal controls and procedures in order to assure that accurate accounting records are maintained and current and complete disclosure of financial results are presented in the financial reports.
Questioned Costs	None
Management Response and Corrective Action	After discussing this finding with the auditors we have taken all the corrective measures in order to record accurately all transactions for each trimester. Responsible Person: Mrs. Wanda I. Del Valle- Federal Programs Director Implementation Date: March 2006.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	05-05
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871); U.S. Department of Housing and Urban Development
Requirement	Cash Management
Statement of Condition	<p>We realized Cash Management Test and after our procedures, we found that the Municipality maintained during the current fiscal year an average cash balance in books of approximately \$183,575. At June 30, 2005, the cash balance in book was \$239,802. Of these funds, \$99,309 was from operating reserve and the remaining \$140,493.31 was not identified by us with respects to its origin.</p> <p>Also, the program maintains a due from Housing Opportunities for Persons with AIDS Program (HOPWA) for the amount of \$30,006. This amount relates to prior and current year Section 8 Housing Choice Vouchers Program financing of HOPWA activities. During the month of February 2005, the Municipality took corrective action against this practice.</p>
Criteria	<p>OMB Common Rules, Subpart C, Section 85.20 (b) (7), requires a cash management system; in order to minimize the time elapsed between the transfer of funds from the U.S. Treasury and disbursement by the grantee.</p>
Cause of Condition	<p>The Municipality did not maintain appropriate cash management procedures in order to request funds to federal agencies only for immediate needs.</p>
Effect of Condition	<p>The PHA did not comply with the OMB Common Rules, Subpart C, Section 85.20, (b) (7).</p>
Recommendation	<p>We recommend to the Municipality's management to instruct the program accountant to review the accounting records and related transactions supporting documents for the current and past years in order to identify the cash balance respects to its origin, and later, to make any necessary adjusting journal entries to correct accounting records.</p>
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 05-05 (continued)

**Management Response
and Corrective Action**

The Municipality, conscious of the situation, has assigned resources to carry out an analysis that details the origin of balances in box. We conducted an audit that included the time period between January 2003 and December 2005. This analysis was finished on February 2006. We're in the process of making any adjusting journal entries to correct accounting records.

Related HOPWA Program Internal Controls have been established to keep both programs funds and payment procedure separated and complying with rules and regulations imposed by the governing laws.

Responsible Person: Mrs. Wanda I. Del Valle-Federal Programs Director

Implementation Date: February 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	05-06
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871); U.S. Department of Housing and Urban Development
Requirement	Special Test – Utility Allowance Schedule
Statement of Condition	The PHA did not maintain an up-to date utility allowance schedule for the audit period ending June 30, 2005. The PHA did not perform a review of the utility rates during the fiscal year to ascertain if there has been a change of ten (10%) percent or more in the utility rate.
Criteria	Code of Federal Regulations 24, Subpart K, Section 982.517 states that the PHA must maintain an up-to-date utility allowance schedule. The PHA must review utility rate data for each utility category each year and must adjust its allowance schedule if there has been a rate change of ten (10) percent or more for a utility category or fuel type since the last time utility allowance was revised.
Cause of Condition	The PHA did not follow the procedures established to review utility rate date each year.
Effect of Condition	The PHA is not in compliance with Code of Federal Regulations 24, Subpart K, Section 982.517.
Recommendation	The PHA should evaluate utility allowance rate each year as established in the federal regulations.
Questioned Costs	None.
Management Response and Corrective Action	On July 29, 2005 we conducted a utilities study. We're in the process of verifying with HUD the procedure to follow as established by Federal Regulations. Also we'll take extreme measures in order to review utility rates each year. Responsible Person: Mrs. Wanda I. Del Valle- Federal Programs Director Implementation Date: July 2006

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	05-07
Program	Section 8 Housing Choice Vouchers Program CFDA (14.871); U.S. Department of Housing and Urban Development
Requirement	Special Test - Housing Quality Standards Inspections
Statement of Condition	During our test we noted that the PHA performs an adequate number of quality control reinspections during the fiscal years 2004-2005. Nevertheless, four (4) of the originals housing quality standards inspections included in the sample were done later than three (3) months from the time of the original inspection.
Criteria	<p>Code of Federal Regulations 24, Subpart I, Sections 982.405 (b) states that the must inspected the unit leased to a family at least annually to determine if the unit meets Housing Quality Standards (HQS) and the PHA must conduct supervisory quality control re-inspections to determine if the work documented in the files conform to program requirements.</p> <p>Code of Federal Regulations 24, Subpart A, 985.2 and the Housing Choice Voucher Guidebook, number 7420.10G, Chapter ten (10), include a guide to determine the minimum size of the PHA's quality control sample.</p>
Cause of Condition	During fiscal year 2004-2005 the Housing Quality Standards inspectors realized the reinspection three (3) months after the original inspection.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Subpart I, Sections 982.405 (b), Subpart A, 985.2 and Housing Choice Voucher Guidebook, number 7420.10G, Chapter ten (10).
Recommendation	We recommend the PHA to assure that the Housing Quality Standard inspectors will minimize the time after the original inspections.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 05-07 (continued)

Questioned Costs None

**Management Response
and Corrective Action** We'll take more rigorous measures in order to minimize the time in
which we conduct the supervisory quality control re-inspections. The
effort began immediately after the audit.

Responsible Person: Mrs. Wanda I. Del Valle- Federal Programs Director

Implementation Date: March 2006

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference Program	05-08 Section 8 Housing Choice Vouchers Program CFDA (14.871) U.S. Department of Housing and Urban Development
Requirement	Special Test - Housing Assistance Payment (HAP)
Statement of Condition	The PHA did not maintain Housing Assistance Payment Register during the fiscal year 2004-2005.
Criteria	Code of Federal Regulations 24, section 982.158 and the Housing Choice Voucher Guidebook, number 7420.11G, Chapter eleven (11). Section 982.158 states that the PHA's are required to maintain a Housing Assistance Payment (HAP) contract register or similar record in which to record the PHA's obligation for monthly HAP's. Housing Choice Voucher Guidebook, number 7420.11G, Chapter eleven (11) states that this record must provide information as to: the name and address of the family, the name and address of the owner, dwelling unit size, the beginning date of the lease term, the monthly rent payable to the owner, monthly rent payable by the family to the owner, and the monthly HAP. The record shall also provide data as to the date the family vacates and the number of days the unit is vacant, if any.
Cause of Condition	The PHA controls and procedures failed to assure that all HAP transactions will be recorded in a HAP Register, as per Regulation.
Effect of Condition	The PHA is not in compliance with Code of Federal Regulations 24, section 982.158 and Housing Choice Voucher Guidebook, number 7420.11G, Chapter eleven (11).
Recommendation	We recommend to the Municipality management to strength controls procedures to assure that all HAP transactions will be recorded in a HAP Register. This Register must provide information as to: the name and address of the family, the name and address of the owner, dwelling unit size, the beginning date of the lease term, the monthly rent payable to the owner, monthly rent payable by the family to the owner, and the monthly HAP. The record shall also provide data as to the date the family vacates and the number of days the unit is vacant, if any.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference **05-08 (Continued)**

Questioned Costs None.

**Management Response
and Corrective Action**

We'll reinforce the controls and the procedures in order to be certain that all HAP transactions are recorded in a HAP Register as required by all federal regulations. We'll design a HAP Register that will contain all the information required following the Auditors recommendation.

Responsible Person: Mrs. Wanda I. Del Valle- Federal Programs Director

Implementation Date: April 2006.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE

SUMMARY SCHEDULE OF PRIOR YEARS AUDIT FINDINGS

YEAR ENDED JUNE 30, 2005

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
04-08	14.871	<p><u>The participant files do not include evidence of the Utility Allowance Schedule.</u></p> <p>Corrective Action was taken.</p>
04-09	14.871	<p><u>Section 8 offices have structural and filtration problems and when it rains, it is impossible for people to enter the building. The program office has structural barriers that prevent easy access for disabled people.</u></p> <p>Partial corrective action has been taken. The Municipality has made structural improvements to the Section 8 office building so that public services are not affected. Nonetheless, the Municipality is searching for a new site where to relocate the program's office.</p>
04-10	14.871	<p><u>The Section 8 Program average cash balance was excessive for the fiscal year ended June 30, 2004.</u></p> <p>Partial corrective action has been taken. The Municipality conscious of the situation has assigned resources to carry out an analysis that details the origin of balance in box. To such effects we are carrying out an audit that includes the period from January 2003 to December 2005, this evaluation will be completed in January of 2006. The Municipality will take all the necessary measures to correct the situation immediately.</p>
04-11	14.871	<p><u>During the audit we observed that there are written procedures of housing quality standards (HQS) but were not implemented or followed.</u></p> <p>Partial corrective action has been taken. Housing Quality Standards (HQS) were implemented. The Municipality performs an adequate number of quality control reinspections. Nonetheless, some of the reinspections are done later than established by Federal Regulation. See Finding Reference 05-07.</p>
04-12	14.871	<p><u>The form HUD-50058 (Family Report) was not in the tenant file.</u></p> <p>Corrective action was taken.</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RIO GRANDE**

SUMMARY SCHEDULE OF PRIOR YEARS AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2005

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
04-13	14.871	<p><u>The tenant's files have various missing documents like: Good Behavior Certificate, Address Evidence, Family photo, Social Security card, and Birth Certificate.</u></p> <p>Corrective action was taken.</p>
04-14	14.871	<p><u>During the audit we observed that the Section 8 program disbursed funds to finance Housing Opportunities for Persons with AIDS (HOPWA) program expenses.</u></p> <p>Partial corrective action has been taken. The Municipality stopped this practice in February 2005 after the issuance of the finding. As of 6/30/05 the program has a due from HOPWA for \$30,006. See Finding Reference 05-05.</p>
04-15	14.218	<p><u>During our examination of ten (10) Disbursement Vouchers we observed the following exceptions: In one (1) case, Voucher for payment does not have the check issuance date, and in eight (8) cases, Voucher for payment do not have the Purchase Order number.</u></p> <p>Corrective action was taken.</p>
03-08	14.871	<p><u>The files did not include evidence of Utility Allowance Schedule.</u></p> <p>Corrective Action was taken.</p>
03-09	14.871	<p><u>Section 8 offices have structural problems that affect service to participants.</u></p> <p>Partial corrective action has been taken. The Municipality has made structural improvements to the Section 8 office building so that public services are not affected. Nonetheless, the Municipality is searching for a new site where to relocate the program's office.</p>

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE
BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION
YEAR ENDED JUNE 30, 2005

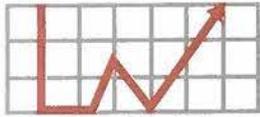
COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

BASIC FINANCIAL STATEMENTS ACCOMPANIED BY
REQUIRED SUPPLEMENTARY INFORMATION

YEAR ENDED JUNE 30, 2005

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of:

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Río Grande
Río Grande, 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 Río Grande, Puerto Rico (Municipality)**, as of and for the year ended June 30, 2005, which collectively comprise the **Municipality's** basic financial statements as listed in the table of contents. These financial statements are the responsibility of the **Municipality's** management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Río Grande, Puerto Rico**, as of June 30, 2005, 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.

INDEPENDENT AUDITORS' REPORT (CONTINUED)

The Management's Discussion and Analysis on pages 3 through 12 and the Budgetary Comparison Schedule-General Fund on page 41 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 21, 2005

Stamp No. 2019495 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2005

This discussion and analysis of the Municipality of Río Grande (the Municipality) financial performance provides an overview of the Municipality's financial activities for the fiscal year ended on June 30, 2005. The Management Discussion and Analysis (MD&A) should be read in conjunction with the accompanying basic financial statements and the accompanying notes to those financial statements. The discussion and analysis includes comparative data for prior year as this information is available for the fiscal year ended on June 30, 2004. This MD & A is prepared in order to comply with such pronouncement and, among other purposes, to provide the financial statements users with the following major information:

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

FINANCIAL HIGHLIGHTS

The following comments about the financial condition and results of operations as reflected in the financial statements prepared for fiscal year 2005 deserve special mention:

1. Total assets of the Municipality amounted to \$37,898,534 which represents a decrease of 33% compared to prior fiscal year.
2. At the end of fiscal year 2005, total liabilities amounted to \$27,425,234. Out of said amount, \$21,241,050 corresponded to long-term liabilities of which \$15,936,000 represented the outstanding balance of bonds issued. The Municipality continued to meet all debt service requirements, most of which was paid from self generated revenues.
3. Total net assets of the Municipality amounted to \$10,473,300 which represents a decrease of 65% compared to prior fiscal year;
4. Total revenues available for the financing of activities as reflected in the Statement of Activities amounted to \$20,280,560, derived from the following sources: \$63,163 charges for services; \$1,743,577 from operating grants and contributions; \$2,040,093 from capital grants and contributions obtained from other sources, and \$16,433,727 from general revenues available.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL HIGHLIGHTS (CONTINUED)

5. Total expenses incurred to afford the cost of all functions and programs as reflected in the Statement of Activities amounted to \$24,377,599;
6. As reflected in the Statement of Activities, the current fiscal year operations contributed to a decrease in the Net Assets figure by \$4,097,039;
7. As of the close of the current fiscal, the Municipality's Governmental Funds reported combined ending fund balances of \$12,761,371;
8. As the end of the current fiscal year the Municipality's general fund balance amounted to \$1,936,159, compared to a fund balance of \$6,854,967 in the prior fiscal year;
9. The actual General Fund budgetary activities resulted in a favorable balance of \$1,075,878.

FUNDAMENTALS OF FINANCIAL STATEMENTS PRESENTATION

The new approach used in the presentation of the financial statements of the Municipality is based on a government-wide view of such statements as well as a presentation of individual funds behavior during fiscal year 2005. The combination of these two perspectives provide the user the opportunity to address significant questions concerning the content of said financial statements, and provide the basis for a comparable analysis of future years performance. The comparative analysis is a meaningful and useful management tool for municipal management in the decision making process.

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

FINANCIAL STATEMENTS COMPONENTS

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

The Statement of Net Assets reflects information of the Municipality as a whole of a consolidated basis and provides relevant information about its financial strength as reflected at the end of the fiscal year. Such financial level is measured as the difference between total assets and liabilities, with the difference between both items reported as net assets. It is important to note that although municipalities as governmental public entities were not created to operate under a profit motive framework, the return on assets performance plays an important role in their financial operations. The higher the increments achieved in net revenues, the higher the capacity to increase the net assets figure either thru additional borrowings or thru internally generated funds. This in turn will benefit the welfare of Río Grande constituents.

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

A brief review of The Statements of Activities of the Municipality at June 30, 2005, shows total expenses incurred to afford the cost of all functions and programs amounted to \$24,377,599. Upon examining the sources of revenues for the financing of said programs, the Statement reflects that \$3,846,833 was derived from the following sources: \$63,163 charges for services; \$1,743,577 from operating grants and contributions; and \$2,040,093 from capital grants and contributions obtained from other sources. General revenues for the year amounted to \$16,433,727. When such figure is added to the \$3,846,833 previously mentioned, total revenues available for the financing of activities amounted to \$20,280,560. There was an excess of expenses over revenues in the amount of \$4,097,039 which contributed with a decrease to the figure of net assets attained at the end of the fiscal year.

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL STATEMENTS COMPONENTS (CONTINUED)

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

INFRASTRUCTURE ASSETS

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

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

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

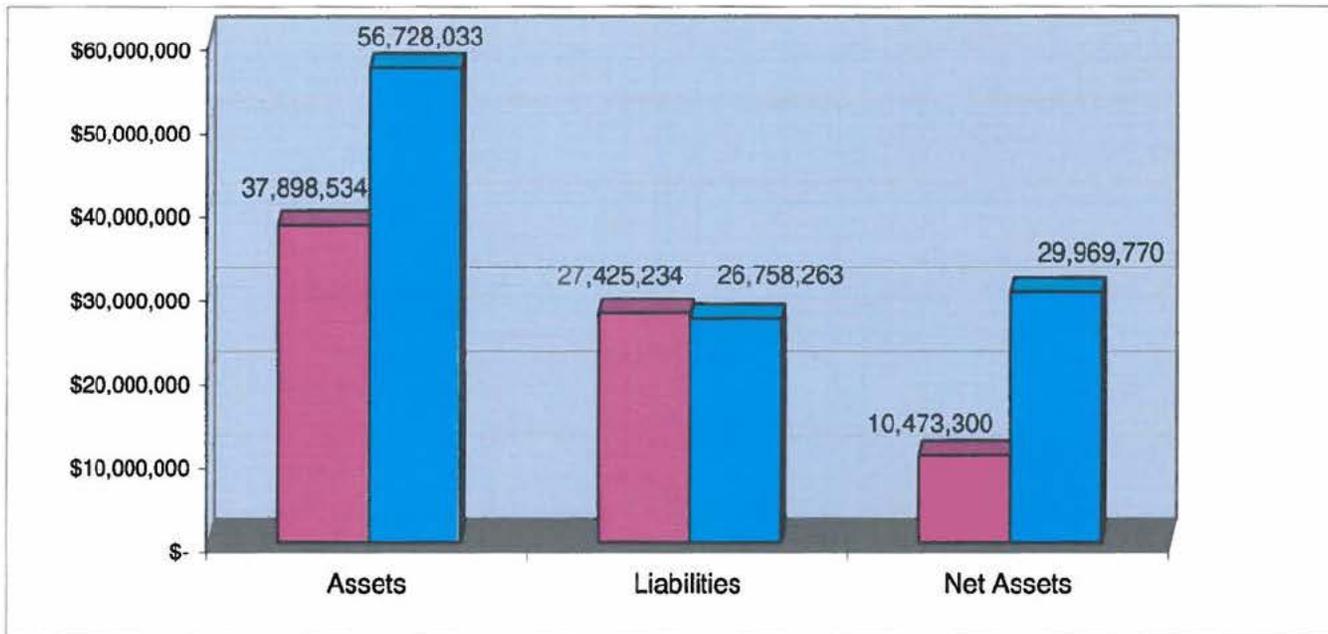
The Statement of Net Assets serves as an indicator of the Municipality's financial position at the end of the fiscal year. In the case of the Municipality of Río Grande, primary government assets exceeded total liabilities by \$10,473,300 at the end of 2005, compared to \$29,969,770 at the end of the previous year, as showed in the following condensed Statement of Net Assets of the Primary Government.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2005

Condensed Statement of Net Assets	2005	2004	Change	%
Current and other assets	\$ 17,435,635	\$ 24,339,761	\$ (6,904,126)	(28%)
Capital assets	20,462,899	32,388,272	(11,925,373)	(37%)
Total assets	37,898,534	56,728,033	(18,829,499)	(33%)
Current and other liabilities	6,184,184	8,536,256	(2,352,072)	(28%)
Long-term liabilities	21,241,050	18,222,007	3,019,043	17%
Total liabilities	27,425,234	26,758,263	666,971	2%
Invested in capital assets, net of related debt	15,775,899	27,400,890	(11,624,991)	(42%)
Restricted	10,494,371	8,683,152	1,811,219	21%
Unrestricted deficit	(15,796,970)	(6,114,272)	(9,682,698)	158%
Total net assets	\$ 10,473,300	\$ 29,969,770	\$ (19,496,470)	(65%)



Changes in Net Assets

The change in net assets is mainly to: (1) the revaluation of the usufruct land owned by the Municipality and (2) the adjustment to property tax receivable.

- (1) As of June 30, 2004, the Municipality valued the usufruct land at market value. However, the usufruct land should have being recognized in books at 1980 values.
- (2) The Municipality recognized all the property tax advances made during the first sixty days for the fiscal year 2004-05 by the CRIM as a receivable. Only ten percent of these collections belonged to prior years.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)

Approximately 62 percent of the Municipality's total revenue came from taxes, while 36 percent resulted from grants and contributions, including federal aid. Charges for Services provided 2 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for general government, health and welfare services, public works, and community development. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

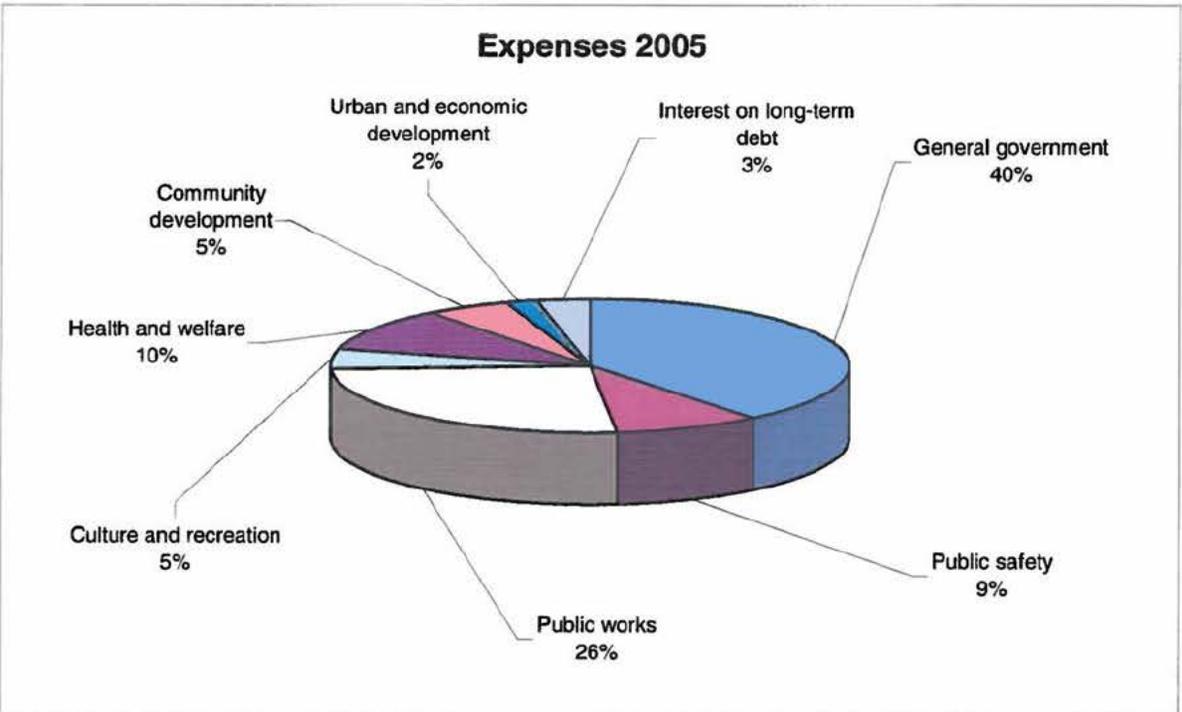
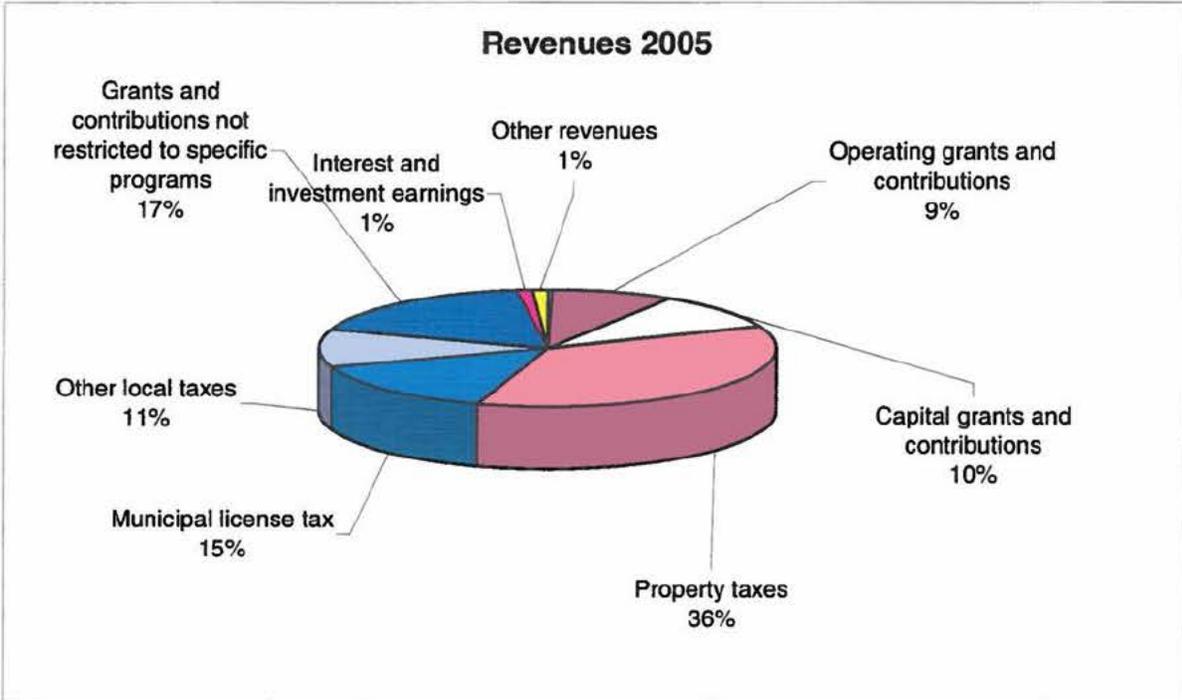
Condensed Statement of Activities	2005	2004	Change	%
Program revenues:				
Charges for services	\$ 63,163	\$ 91,096	\$ (27,933)	(31%)
Operating grants and contributions	1,743,577	1,350,789	392,788	29%
Capital grants and contributions	2,040,093	3,024,699	(984,606)	(33%)
General revenues:				
Property taxes	7,309,588	7,297,629	11,959	-
Municipal license tax	2,959,724	2,346,971	612,753	26%
Other local taxes	2,186,558	3,324,269	(1,137,711)	(34%)
Grants and contributions not restricted to specific programs	3,501,697	3,529,383	(27,686)	(1%)
Interest and investment earnings	271,371	162,408	108,963	67%
Other revenues	204,789	1,413,268	(1,208,479)	(86%)
Total revenues	20,280,560	22,540,512	(2,259,952)	(10%)
Expenses:				
General government	9,563,927	4,642,895	4,921,032	106%
Public safety	2,218,604	3,379,433	(1,160,829)	(34%)
Public works	6,278,998	2,707,279	3,571,719	132%
Culture and recreation	1,268,483		1,268,483	100%
Health and welfare	2,446,071	4,372,696	(1,926,625)	(44%)
Community development	1,336,009		1,336,009	100%
Urban and economic development	449,208	1,691,635	(1,242,427)	(73%)
Interest on long-term debt	816,299	878,211	(61,912)	(7%)
Total expenses	24,377,599	17,672,149	6,705,450	38%
Change in net assets	(4,097,039)	4,868,363	(8,965,402)	(184%)
Net assets, beginning of year, as restated	14,570,339	25,101,407	(10,531,068)	(42%)
Net assets, end of year	\$ 10,473,300	\$ 29,969,770	\$(19,496,470)	(65%)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE (CONTINUED)



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$12,761,371, a decrease of \$1,690,512 in comparison with the prior year. There are reservations of fund balance amounting to \$11,506,811. This is the fund balance that it is not available for new spending because it has already been committed 1) \$656,160 to liquidate contracts and purchase orders of the prior fiscal year, 2) \$7,471,250 to pay debt service, 3) \$3,155,871 to pay for capital projects, and 4) \$223,530 for other purposes.

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2005, the general fund has an undesignated fund balance of \$1,254,560.

GENERAL FUND BUDGETARY HIGHLIGHTS

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

The actual General Fund budgetary activities resulted in a favorable balance of \$1,075,878, caused mainly due to unexpected variances in revenue collections from miscellaneous sources.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

CAPITAL ASSETS AND DEBT ADMINISTRATION (CONTINUED)

The Municipality's investment in capital assets as of June 30, 2005, amounts to \$35,420,936, net of accumulated depreciation of \$14,958,037 (including depreciation charges for the year totaled \$750,352), leaving a net book value of \$20,462,899. This investment in capital assets includes land, construction in progress, buildings, improvements, equipment, infrastructure and vehicles. Infrastructure assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The Municipality finances a significant portion of its construction activities through bond or notes issuances. The proceeds from bond and notes issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2005, the Municipality has \$1,036,659 of unexpended proceeds mainly from bonds issuances that are committed to future construction activities.

Debt Administration

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2005

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal and state grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal and State grant revenues may vary if new grants are available but the revenue also is very predictable. Those factors were considered when preparing the Municipality's budget for the fiscal year 2005-2006.

FINAL COMMENTS

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

The Municipality's management is committed to a continued improvement in the confection of a budget that will response to the needs of the public and private sectors in accordance with its permissible revenues levels. Such has been the case of the financial operation corresponding to fiscal year 2005. It further contemplates to maintain or improve its current levels of Net Assets as indicative of a strong financial position which has been identified as one of the main short and long-term objectives of the Municipality.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer at P.O. Box 847, Río Grande, PR 00745 or call (787) 887-2370.

Commonwealth of Puerto Rico
Municipality of Río Grande
Statement of Net Assets
June 30, 2005

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 7,034,422
Cash with fiscal agent	9,139,993
Accounts receivable:	
Municipal License Tax	4,000
Property tax	785,628
Intergovernmental	436,794
Interest	34,798
Capital assets	
Land, improvements, and construction in progress	7,355,045
Other capital assets, net of depreciation	13,107,854
Total capital assets	<u>20,462,899</u>
Total assets	<u>37,898,534</u>
Liabilities	
Accounts payable and accrued liabilities	2,098,324
Due to other governmental entities	179,324
Deferred revenues:	
Municipal license tax	1,630,322
Federal grant revenues	715,683
Interest payable	356,280
Noncurrent liabilities:	
Due within one year	1,204,251
Due in more than one year	21,241,050
Total liabilities	<u>27,425,234</u>
Net Assets	
Invested in capital assets, net of related debt	15,775,899
Restricted for:	
Capital projects	3,155,871
Debt service	7,114,970
Other purposes	223,530
Unrestricted (deficit)	<u>(15,796,970)</u>
Total net assets	<u>\$ 10,473,300</u>

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

**Commonwealth of Puerto Rico
Municipality of Río Grande
Statement of Activities
For the Year Ended June 30, 2005**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 9,563,927	\$ 11,968	\$ -	\$ 293,516	\$ (9,258,443)
Public safety	2,218,604	21,262	160,216		(2,037,126)
Public works	6,278,998	29,933	72,994	156,302	(6,019,769)
Health and welfare	2,446,071		999,605	10,810	(1,435,656)
Culture and recreation	1,268,483		67,698	237,712	(963,073)
Economic development	260,871		429,956		169,085
Community development	1,336,009			1,341,753	5,744
Urban development	188,337				(188,337)
Education			13,108		13,108
Interest on long-term debt	816,299				(816,299)
Total governmental activities	\$ 24,377,599	\$ 63,163	\$ 1,743,577	\$ 2,040,093	(20,530,766)
General revenues:					
Property taxes					7,309,588
Municipal license tax					2,959,724
Other local taxes					2,186,558
Grants and contributions not restricted to specific programs					3,501,697
Interest and investment earnings					271,371
Miscellaneous					204,789
Total general revenues					16,433,727
Change in net assets					(4,097,039)
Net assets - beginning, as restated					14,570,339
Net assets - ending					\$ 10,473,300

**Commonwealth of Puerto Rico
Municipality of Rio Grande
Balance Sheet
Governmental Funds
June 30, 2005**

	General Fund	Special Revenue Fund Federal Grants	Capital Projects Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Assets						
Cash and cash equivalents	\$ 3,686,249	\$ 602,168	\$ 2,275,912	\$ -	\$ 470,093	\$ 7,034,422
Cash with fiscal agent	901,998	398	1,036,659	7,200,938		9,139,993
Accounts receivable:						
Municipal license tax	4,000					4,000
Property Tax	64,964			296,410		361,374
Intergovernmental		373,312			63,482	436,794
Interest	20,700			14,098		34,798
Due from other funds	603,281				30,006	633,287
Total assets	\$ 5,281,192	\$ 975,878	\$ 3,312,571	\$ 7,511,446	\$ 563,581	\$ 17,644,668
Liabilities and Fund Balances						
Liabilities :						
Accounts payable and accrued liabilities	\$ 1,535,387	\$ 32,594	\$ 156,700	\$ -	\$ -	\$ 1,724,681
Due to other governmental entities	179,324					179,324
Due to other funds		477,334		40,196	115,757	633,287
Deferred revenues:						
Municipal license tax	1,630,322					1,630,322
Federal grant revenues		465,950			249,733	715,683
Total liabilities	3,345,033	975,878	156,700	40,196	365,490	4,883,297
Fund balances:						
Reserved for:						
Encumbrances	656,160					656,160
Capital projects			3,155,871			3,155,871
Debt service fund				7,471,250		7,471,250
Other purposes	25,439					25,439
Reserved reported in nonmajor funds:						
Other purposes					198,091	198,091
Unreserved:						
Undesigned	1,254,560					1,254,560
Total fund balances	1,936,159		3,155,871	7,471,250	198,091	12,761,371
Total liabilities and fund balances	\$ 5,281,192	\$ 975,878	\$ 3,312,571	\$ 7,511,446	\$ 563,581	
Amounts reported for governmental activities in the statement of net assets are different because:						
Accrual basis of accounting accounts receivable recognized in government-wide financial statements						424,254
Accrual basis of accounting accounts payable recognized in government-wide financial statements						(373,643)
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds						20,462,899
Long-term liabilities, including accrued interest payable, are not due and payable in the current period, and therefore, are not reported in the funds						(22,801,581)
Net assets of governmental activities						\$ 10,473,300

Commonwealth of Puerto Rico
Municipality of Rio Grande
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2005

	General Fund	Special Revenue Fund Federal Grants	Capital Project Fund - State & Local Grants	Debt Service Fund	Other Governmental Funds	Total Governmental Funds
Revenues						
Property taxes	\$ 5,665,999	\$ -	\$ -	\$ 1,682,792	\$ -	\$ 7,348,791
Municipal license taxes	2,887,594				72,130	2,959,724
Licenses, permits and other local taxes	2,198,526					2,198,526
Intergovernmental	3,501,697		404,824		684,716	4,591,237
Fines and forfeitures	21,262					21,262
Rent of property	29,933					29,933
Interest	271,371					271,371
Federal grants		1,787,916			471,044	2,258,960
Miscellaneous	180,395	1,551	7,226		157,271	346,443
Total revenues	14,756,777	1,789,467	412,050	1,682,792	1,385,161	20,026,247
Expenditures						
Current						
General government	6,550,252		3,673		50,844	6,604,769
Public safety	2,064,497	34			136,251	2,200,782
Public works	5,533,708	39,433	236,486		430,948	6,240,575
Health and welfare	1,370,467	389,967	41,612		619,131	2,421,177
Culture and recreation	645,186	20,768	329,557		14,750	1,010,261
Economic development					260,871	260,871
Community development		1,341,753				1,341,753
Urban development			188,337			188,337
Debt service:						
Principal				651,000		651,000
Interest				826,740		826,740
Total expenditures	16,164,110	1,791,955	799,665	1,477,740	1,512,795	21,746,265
Excess (deficiency) of revenues over (under) expenditures	(1,407,333)	(2,488)	(387,615)	205,052	(127,634)	(1,720,018)
Other financing sources (uses)						
Transfers in			1,277,451	81,750	144,655	1,503,856
Transfers out	(1,107,837)	(174,539)	(47,630)		(173,850)	(1,503,856)
Total other financing sources (uses)	(1,107,837)	(174,539)	1,229,821	81,750	(29,195)	-
Net change in fund balances	(2,515,170)	(177,027)	842,206	286,802	(156,829)	(1,720,018)
Fund balance, beginning as restated	4,451,329	177,027	2,313,665	7,184,448	354,920	14,481,389
Fund balance, ending	\$ 1,936,159	\$ -	\$ 3,155,871	\$ 7,471,250	\$ 198,091	\$ 12,761,371

**Commonwealth of Puerto Rico
Municipality of Río Grande
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2005**

Net Change in Fund Balances - Total Governmental Funds \$ (1,720,018)

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

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period. 1,140,443

Depreciation expense on capital assets is reported in the Government-Wide Statements of Activities and Change in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds. (750,353)

Interest expense on long-term debt was reported in the Government-Wide Statement of Activities and Change in Net Assets, but it did not require the use of current financial resources. Therefore, interest expense was not reported as expenditures in Governmental Funds. The following amount represented the change in accrued interest from prior year. 10,441

Bonds and notes proceeds provides current financial resources to Governmental Funds, but issuing debt increase long-term liabilities in the Government-Wide Statement of Net Assets. Repayment of bonds and notes principal is an expenditure in Governmental Funds, but the repayment reduces long-term liabilities in the Government-Wide Statement of Net Assets. This is the amount paid in the current year. 651,000

Repayment of long term Treasury Department debt is an expenditure in Governmental Funds, but the repayment reduces long-term debt in the Government-Wide Statement of Net Assets. This is the amount paid in the current year. 27,015

Repayment of long term property tax advance debt is an expenditure in Governmental Funds, but the repayment reduces long-term property tax advance debt in the Government-Wide Statement of Net Assets. The following amount represent the change in long-term property tax advance debt from prior year. (2,203,454)

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenue in the funds. The following amount represents the change in this revenues from prior year. (39,203)

Some expenses reported in the Governmental Funds do not require the use of current financial resources and, therefore, are not reported as expenses in the Statement of Activities. The following amount represents the change in this expenses from prior year. (37,157)

Long-term federal cost disallowances are reported in the Governmental-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, federal cost disallowances are not reported as expenditures in Government Funds. The following amount represent the change in long-term federal cost disallowances from prior year. (49,385)

Long-term claims and judgements are reported in the Governmental-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, claims and judgments are not reported as expenditures in Government Funds. The following amount represent the change in long-term claims and judgments from prior year. (1,184,338)

Account payables reported in the Government-Wide Statement of Activities and Change in Net Assets but not reported as in the Governmental Funds because they do not require the use of current financial resources. This is the amount reported in the current period. (373,643)

Long-term compensated absences are reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, long-term compensated absences were not reported as expenditures in Governmental Funds. The following amount represent the change in long-term compensated absences from prior year. 431,613

Change in Net Assets of Governmental Activities \$ (4,097,039)

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2005

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The **Municipality of Río Grande** (the Municipality) was founded on the year 1840. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a sixteen member Municipal Legislature who are elected for a four-year term.

The Municipality provides a full range of services for its citizens. These services include public safety, public works, culture and recreation, health and welfare, community development, education, and other miscellaneous services.

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

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's and Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. The Statement was adopted as of July 1, 2002. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

As part of this Statement, there is a new reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). This requirement permits an optional four-year delay for implementation to fiscal year ended on June 30, 2007. The Municipality has elected to delay the capitalization of infrastructure.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

A. Component Units

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, The Financial Reporting Entity, of the GASB, as amended by GASB Statement No. 39. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

B. Government-wide and fund financial statements

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

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

Special Revenue Fund – Federal Grants- is the accounting entity in which revenues derived from federal grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal statutes.

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

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

C. Financial reporting presentation

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

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

Special Revenue Fund - Local and State Grants - Special Revenue Funds are used to account for revenues derived from local funds, state grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Section 8 - Special Revenue Funds are used to account for revenues derived from section 8 choice voucher program. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Special Revenue Fund - Federal Grants - Special Revenue Funds are used to account for revenues derived from federal grants. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Projects Fund - State and Local Grants - Capital Projects Fund are used to account for financial resources used for the acquisition or construction of major capital facilities.

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

D. Measurement focus, basis of accounting and financial presentation

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

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

Property taxes, franchise taxes, licenses, rent, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

Private-sector standards of accounting and financial reporting issue prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

E. Assets, liabilities and net assets

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

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

- 2. Receivables and payables-** Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivable in the special revenue or capital project funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded or state funded programs.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

3. Inventories- Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.

4. Capital assets- Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

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

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

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

<u>Description</u>	<u>Useful Life</u>	<u>Capitalization threshold</u>
Buildings and site improvements	30 to 50 years	\$1
Infrastructure	20 to 50 years	\$1
Works of art	10 years	\$1
Vehicles	8 years	\$1
Furniture and fixtures	5 to 20 years	\$25
Machinery and equipment	5 to 20 years	\$25

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

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

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

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

7. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.

8. **Reservation of fund balance-** Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:

- a. **Capital Projects-** Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
- b. **Encumbrances-** Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
- c. **Other Purposes-** Represents net assets available for specific use and/or legally segregated for other specific future use.
- d. **Debt Service Fund-** Represents net assets available to finance future debt service payments.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

9. Interfund and intra-entity transactions- The Municipality has the following types of transactions among funds:

- a. **Operating Transfers-** Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
- b. **Intra-Entity Transactions-** Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.

10. Risk financing- The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico.

Cost of insurance allocated to the Municipality and deducted from the gross property tax collections by the Municipal Revenue Collection Center ("CRIM") for the year ended June 30, 2005 amounted to approximately \$139,763. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$300,272 for workers compensation insurance covering all municipal employees.

11. Reconciliation of Government-wide and Fund Financial Statements

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

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

The details of this reconciliation are as follows:

		<u>Total Net Assets</u> <u>Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 20,462,899	
Deduct:		
Bonds and notes payable	<u>(4,687,000)</u>	\$ 15,775,899
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		3,155,871
<u>Net assets restricted for debt service</u>		
Fund balance restricted for debt service	7,471,250	
Deduct:		
Interest Payable	(356,280)	7,114,970
<u>Net assets restricted for other purposes</u>		
Other governmental funds—fund balance restricted for other purposes		198,091
<u>Net assets unrestricted (deficit)</u>		
General fund – total fund balance:	\$ 1,936,159	
Add:		
Accrual basis accounts receivable	424,254	
Deduct:		
Accrual basis accounts payable	(373,643)	
Bonds Payable	(11,249,000)	
Property Tax-Treasury	(193,722)	
Property Tax-Advance	(517,214)	
CRIM-Law 146	(1,686,241)	
Compensated absences	(1,830,789)	
Claims and judgments	(1,509,068)	
Reserve for federal cost disallowances	<u>(772,267)</u>	<u>(15,771,531)</u>
Total net assets - governmental activities		<u>\$ 10,473,300</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

2. DEPOSITS

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

The Municipality's bank balances in commercial banks of \$3,686,249 in the general fund, \$602,168 in the special revenue fund - federal grants, and \$2,275,912 in the capital projects fund - state and local grants were fully collateralized at June 30, 2005. In the other governmental funds there were deposits with commercial banks of \$470,093 that were fully collateralized.

The deposits at GDB of \$901,998 in the general fund, the \$398 in the special revenue fund - federal grants, the \$1,036,659 in the capital projects fund - state and local grants, and the \$7,200,938 that is restricted for debt service fund, are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

A. *Municipal License Tax*- The Municipality impose a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2005, the tax rates were as follows:

1. Financial business- 1.50% of gross revenues
2. Other organizations- 0.50% of gross revenues

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2005, net of allowance for uncollectible.

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

3. RECEIVABLES (CONTINUED)

B. *Intergovernmental Receivables*- Intergovernmental receivable in special revenue fund – federal grants represent expenditures incurred not yet reimbursed by the federal government. Following is a detail of the intergovernmental receivable:

<u>Program Description</u>	<u>Amount</u>
Community Development Block Grant – Entitlement Grant	\$ 111,313
Child Care and Development Block Grant	174,550
Community Service Block Grant	<u>87,449</u>
Total	<u>\$ 373,312</u>

Intergovernmental receivable in the debt service fund represents the amounts due from the CRIM resulting from the excess of current year property tax collections over current year advances. Following is a detail of the intergovernmental receivables:

<u>Governmental Entity</u>	<u>Amount</u>
Municipal Revenue Collection Center (CRIM)	<u>\$ 296,410</u>
Total	<u>\$ 296,410</u>

Intergovernmental receivable in the other governmental funds represent expenditures incurred not yet reimbursed by other governmental entities. Following is a detail of the intergovernmental receivable:

<u>Program Description</u>	<u>Amount</u>
Commonwealth of Puerto Rico-Department of Labor and Human Resources- Law 52 Grant	<u>\$ 63,482</u>
Total	<u>\$ 63,482</u>

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2005, and interfund transfers during the fiscal year ended at June 30, 2005, are summarized as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

4. INTERFUND TRANSACTIONS (CONTINUED)

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Special Revenue Fund - Federal Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	\$ 447,328
General Fund	Debt Service Fund	Interest Revenue	40,196
General Fund	Other Governmental Funds	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	115,757
Other Governmental Funds	Special Revenue Fund - Federal Grants	Payroll and related accruals paid and not reimbursed, and other reimbursable expenditures	<u>30,006</u>
Total			<u>\$ 633,287</u>

b. Transfer in/out to other fund

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	\$ 881,432
General Fund	Debt Service Fund	Debt retirement	81,750
General Fund	Other Governmental Funds	Transfer of funds to Other Governmental Funds	144,655
Special Revenue Fund - Federal Grants	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	174,539
Capital Projects Fund - State and Local Grants	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	47,630
Other Governmental Funds	Capital Projects Fund - State and Local Grants	Transfer of funds for capital outlays	<u>173,850</u>
Total			<u>\$ 1,503,856</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

5. CAPITAL ASSETS

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2005, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

Governmental Activities:	Balance July 1, 2004	Additions	Retirements	Balance June 30, 2005
Capital asset, not being depreciated:				
Land	\$ 1,194,589	522		1,195,111
Construction in progress	<u>5,704,402</u>	<u>455,531</u>	-	<u>6,159,933</u>
Total capital assets not being depreciated	<u>6,898,991</u>	<u>456,053</u>	-	<u>7,355,044</u>
Capital assets, being depreciated:				
Buildings and building improvements	15,041,086	3,950		15,045,036
Infrastructure	1,907,946	293,516		2,201,462
Infrastructure improvements	4,624,953			4,624,953
Equipment	1,531,598	187,639		1,719,237
Furnishing		35,413		35,413
Computers		8,178		8,178
Vehicles	<u>4,275,919</u>	<u>155,694</u>	-	<u>4,431,613</u>
Total capital assets being depreciated	<u>27,381,502</u>	<u>684,390</u>	-	<u>28,065,892</u>
Less accumulated depreciation for:				
Buildings and building improvements	(5,002,378)	(303,121)		(5,305,499)
Infrastructure	(558,427)	(74,523)		(632,950)
Infrastructure improvements	(4,597,570)	(5,868)		(4,603,438)
Equipment	(792,941)	(108,924)		(901,865)
Furnishing		(1,249)		(1,249)
Computers		(50)		(50)
Vehicles	<u>3,256,369</u>	<u>(256,617)</u>	-	<u>(3,512,986)</u>
Total accumulated depreciation	<u>14,207,685</u>	<u>(750,352)</u>	-	<u>(14,958,037)</u>
Total capital assets being depreciated, net	<u>13,173,817</u>	<u>(65,962)</u>	-	<u>13,107,855</u>
Governmental activities capital assets, net	<u>\$ 20,072,808</u>	<u>390,091</u>	-	<u>20,462,899</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

5. CAPITAL ASSETS (CONTINUED)

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

Governmental activities:

General government	\$ 70,740
Public safety	129,711
Public works	253,164
Culture and recreation	271,843
Health and welfare	<u>24,894</u>

Total depreciation expense-governmental activities **\$ 750,352**

6. PROPERTY TAXES

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

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30. However, if advances exceed the amount actually collected by the CRIM, a payable to the CRIM is recorded at June 30. The CRIM issued the final liquidation noting that the advances exceeded collections by \$208,230. This excess will not be funded with available expendable financial resources at June 30, 2005. Based on this, such amount was presented in the government-wide financial statements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

6. PROPERTY TAXES (CONTINUED)

The Municipality entered into an agreement with the Commonwealth of Puerto Rico for the repayment of excess property tax advances. As of June 30, 2005, the related unpaid property tax advances presented in the statement of net assets amounted to approximately \$193,722.

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

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

On June 26 1997, Public Law Num. 21 was enacted authorizing the CRIM, among other things, to sell the property tax receivables related to taxpayers who owned property taxes from 1974 to 1996. Such property tax receivables were purchased by the Public Financing Corporation, a subsidiary of the Government Development Bank of Puerto Rico (GDB) using the proceeds of a bond issuance executed for such purposes. Said Law imposed the CRIM the obligation to replace uncollectible property tax receivables with any valid property tax receivable o equivalent in money. Subsequent to the approval of the Law and to the sale transaction, it was detected that a substantial percentage of the receivables sold were uncollectible. In order to protect the economic damage to the financial structure of municipalities caused by the substitution of uncollectible tax receivables with sound collectible receivables, on October 11, 2001, Public Law 146 was approved and enacted. Through this Law, the CRIM was authorized to obtain a loan from any qualified financial institution and pay in advance the outstanding balance of the bonds issued and any related cost incurred for the purchase by the Public Financing Corporation (a GDB subsidiary) of the tax receivables. The loan is being paid by the municipalities thru a 30 year long term financing negotiated by the CRIM with GDB on behalf of such municipalities as authorized by the indicated Law. As of June 30 2005, the related unpaid property tax advances presented in the Statement of Net Assets amounted to approximately \$1,686,241.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

6. PROPERTY TAXES (CONTINUED)

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

The annual tax rate is 8.23% for real property and 6.23% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.40% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund.

7. DUE TO OTHER GOVERNMENTAL ENTITIES:

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

<u>Governmental Entity</u>	<u>Amount</u>
Puerto Rico Telephone Company	\$ 91,165
Puerto Rico Aqueduct and Sewer Authority	48,126
General Services Administration	22,121
Department of Labor and Human Resources	<u>17,912</u>
Total	<u>\$ 179,324</u>

8. DEFERRED REVENUES

A. Municipal License Tax- The deferred revenues of approximately \$1,630,322 in the general fund relates to municipal license tax collected in fiscal year 2004-05 that will be earned in fiscal year 2005-06.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

8. DEFERRED REVENUES (CONTINUED)

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

<u>Program Description</u>	<u>Amount</u>
Section 8 Housing Choice Voucher	\$ 249,733
Wildlife Restoration	38,736
Housing Opportunities for Persons with AIDS	48,150
Public Assistance Grant	331,297
Urban Development Action Grant	14,368
Grants for Supportive Services and Senior Centers	12,036
Community Development Block Grant	9,254
Others	<u>12,109</u>
Total	<u>\$ 715,683</u>

9. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2005, was as follows:

<u>Description</u>	<u>Beginning Balance</u>	<u>Borrowings or Additions</u>	<u>Payments or Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds Payable	\$ 16,587,000	\$ -	\$ (651,000)	\$15,936,000	\$ 579,000
Property Tax-Treasury	220,737		(27,015)	193,722	28,397
Property Tax-Advance		517,214		517,214	308,984
CRIM - Law 146		1,686,241		1,686,241	
Compensated absences	2,262,402		(431,613)	1,830,789	94,803
Claims and Assessments	324,731	1,451,504	(267,167)	1,509,068	
Reserve for federal cost disallowances	722,882	165,154	(115,769)	772,267	193,067
Obligation under capital leases	<u>7,879</u>	<u>-</u>	<u>(7,879)</u>	<u>-</u>	<u>-</u>
Total	<u>\$20,125,631</u>	<u>\$3,820,113</u>	<u>\$(1,500,443)</u>	<u>\$22,445,301</u>	<u>\$1,204,251</u>

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

9. LONG-TERM LIABILITIES (CONTINUED)

2. Bonds payable- The Municipality issues general and special obligation bonds to provide funds for the acquisition and construction of major capital facilities. Bonds payable outstanding at June 30, 2005 are as follows:

<u>Type of bonds</u>	<u>Maturity Date</u>	<u>Original Amount</u>	<u>Range of Interest Rates</u>	<u>Balance at June 30, 2005</u>
1991-Series	7/1/2005	\$ 155,000	6.26%	\$ 20,000
1995-Series	1/1/2019	1,187,000	4.50%	897,000
1996-Series	7/1/2020	1,045,000	5.93% to 6.63%	865,000
1996-Series	7/1/2020	1,715,000	5.93% to 6.63%	1,430,000
1998-Series	7/1/2012	355,000	5.42% to 6.04%	240,000
2002-Series	7/1/2026	5,105,000	5.00% to 8.00%	4,885,000
2002-Series	7/1/2016	1,400,000	2.89% to 4.91%	1,235,000
2002-Series	7/1/2008	1,055,000	2.89% to 3.88%	675,000
2003-Series	7/1/2027	4,746,000	6.50%	4,579,000
2003-Series	7/1/2027	1,175,000	6.50%	<u>1,110,000</u>
Total general obligation bonds				<u>\$15,936,000</u>

These bonds, except the 2003 Series \$1,175,000 bond, are payable from the ad valorem property tax of 1.40% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes. The 2003 Series \$1,175,000 bond is payable with General Fund resources.

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

<u>Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 579,000	\$ 805,723
2007	597,000	997,157
2008	647,000	964,375
2009	696,000	928,154
2010	547,000	892,269
2011-2015	3,299,000	3,885,710
2016-2020	3,942,000	2,699,349
2021-2025	3,563,000	1,392,943
2026-2030	<u>2,066,000</u>	<u>192,488</u>
Total	<u>\$ 15,936,000</u>	<u>\$ 12,758,168</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

9. LONG-TERM LIABILITIES (CONTINUED)

3. **Compensated absences-** The government-wide statement of net assets includes approximately \$979,019 of accrued sick leave benefits, and approximately \$851,770 of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.
4. **Federal cost disallowances-** At June 30, 2005, the accompanying statement of net assets presents a reserve for ineligible and unsupported costs under federally assisted programs amounting to \$772,267.

10. PENSION PLAN

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

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

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

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

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

10. PENSION PLAN (CONTINUED)

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$ 550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions during the year ended June 30, 2005 amounted to approximately \$561,185.

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

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan.

Additional information on the Retirement System is provided in its financial statements for the year ended June 30, 2005, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940.

11. RISK MANAGEMENT

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

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

12. CAPITAL ASSETS REPORTED VALUE

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

13. CONTINGENCIES

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities.

With respect to pending and threatened litigation, the Municipality has reported liabilities of approximately \$1,509,068 for awarded and anticipated unfavorable judgments. This amount was included in the financial statements and represents the amount estimated as probable liability or a liability with a fixed or expected due date, which will require future available financial resources for its payment.

It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

14. BEGINNING FUND BALANCES RESTATEMENT

The following restatements have been made in the financial statements, which are reported as an adjustment to beginning fund balance or net assets:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2005

14. BEGINNING FUND BALANCES RESTATEMENT (CONTINUED)

Adjustments to fund balance of governmental funds in the fund financial statements:

General Fund

Corrections to the property tax receivable	\$ (991,448)
Reclassification of funds from General Fund to Special Revenue and Capital Projects Funds, to conform with the Current Basic Financial Statements presentation	(1,100,449)
Accrued liabilities not previously recorded	(270,690)
Others adjustments	<u>(41,051)</u>
Total decrease in fund balance	<u>(2,403,638)</u>

Special Revenue Fund - Federal Grants

Deferred revenue not previously recorded	<u>140,779</u>
Total increase in fund balance	<u>140,779</u>

Capital Projects Fund - State & Local Grants

Reclassification of funds from General Fund to Capital Projects Funds, to conform with the Current Basic Financial Statements presentation	493,136
Revenue earned recorded as deferred	477,438
Reclassification of special revenue fund - federal grant classified in capital projects fund in the previous year	194,098
Others adjustments	<u>(9,070)</u>
Total increase in fund balance	<u>1,155,602</u>

Debt Service Fund

Corrections to the property tax receivable	(193,192)
Reclassification of accounts payable	837,259
Accrued revenue not previously recorded	<u>91,797</u>
Total increase in fund balance	<u>735,864</u>

Other Governmental Funds

Reclassification of funds from General Fund to Special Revenue Funds, to conform with the Current Basic Financial Statements presentation	607,312
Reclassification of deferred recognized as revenue	(252,285)
Others adjustments	<u>45,872</u>
Total increase in fund balance	<u>400,899</u>

Net increase in fund balance, governmental funds

\$ 29,506

Adjustments to net assets in the government-wide financial statement

Corrections to the property tax receivable	\$ (3,628,215)
Change in land reported value	(12,285,721)
Others adjustments	<u>514,505</u>
Total decrease in net assets	<u><u>\$(15,399,431)</u></u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE**

BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2005

	<u>Budgeted Amounts</u>		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 5,595,337	\$ 5,595,337	\$ 5,672,199	\$ 76,862
Fines and forfeiture	3,000	3,000	21,262	18,262
Municipal license tax	2,251,500	2,251,500	2,913,593	662,093
Licenses, permits and other local taxes	3,315,000	3,315,000	2,198,526	(1,116,474)
Intergovernmental	3,508,831	3,508,831	3,501,697	(7,134)
Interest	175,000	175,000	231,445	56,445
Rent of property	30,000	30,000	29,933	(67)
Miscellaneous	<u>235,000</u>	<u>235,000</u>	<u>180,395</u>	<u>(54,605)</u>
Total revenues	<u>15,113,668</u>	<u>15,113,668</u>	<u>14,749,050</u>	<u>(364,618)</u>
Budget carryover (1)		2,919,244	2,919,244	
Total revenues after carryover	<u>15,113,668</u>	<u>18,032,912</u>	<u>17,668,294</u>	<u>(364,618)</u>
EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING USES:				
Current:				
General government	4,972,926	6,094,482	5,664,043	430,439
Public safety	2,382,442	2,455,060	2,084,933	370,127
Public works	5,574,962	6,296,672	5,794,128	502,544
Health and welfare	1,430,940	1,441,822	1,375,806	66,016
Culture and recreation	653,623	846,101	791,756	54,345
Operating transfer to other funds	<u>98,775</u>	<u>898,775</u>	<u>881,750</u>	<u>17,025</u>
Total expenditures, encumbrances and other financing uses	<u>15,113,668</u>	<u>18,032,912</u>	<u>16,592,416</u>	<u>1,440,496</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, ENCUMBRANCES AND OTHER FINANCING SOURCES (USES)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,075,878</u>	<u>\$ 1,075,878</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 17,668,294
Differences-budget to GAAP:				
Budget Carryover				(2,919,244)
GAAP adjustments to revenues				<u>7,727</u>
Total revenues and other financing sources as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 14,756,777</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 16,592,416
Differences-budget to GAAP:				
Non-budgeted expenditures				212,129
Prior year encumbrances recorded as current year expenditures for GAAP basis				897,475
Current year encumbrances recorded as expenditures for budgetary purposes				(656,160)
No budgeted transfer out				<u>226,087</u>
Total expenditures and other financing uses as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 17,271,947</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF RÍO GRANDE

NOTES TO BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2005

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

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

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2005 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2005.