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AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL

AREA DE ARCHIVO DIGITAL

MUNICIPIO DE SAN JUAN

AUDITORIA 2004-2005

30 DE JUNIO DE 2005

GOVERNMENT OF PUERTO RICO
SECRETARÍA DE ECONOMÍA

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GOVERNMENT OF PUERTO RICO
SECRETARÍA DE ECONOMÍA

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Municipality of San Juan, Puerto Rico

***OMB Circular A-133 Audit for the
Year Ended June 30, 2005,
and Independent Auditors' Report***

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MUNICIPALITY OF SAN JUAN, PUERTO RICO

OMB CIRCULAR A-133 AUDIT FOR THE YEAR ENDED JUNE 30, 2005

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MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART I

**BASIC FINANCIAL STATEMENTS, REQUIRED SUPPLEMENTARY
INFORMATION AND ADDITIONAL SUPPLEMENTARY
INFORMATION AS OF AND FOR THE YEAR ENDED JUNE, 30, 2005,
AND INDEPENDENT AUDITORS' REPORT**

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of the Legislature of
Municipality of San Juan, Capital City of Puerto Rico
San Juan, 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 San Juan, Capital City of Puerto Rico (the "Municipality"), as of and for the year ended June 30, 2005, which collectively comprise the Municipality's basic financial statements. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express an opinion on the respective financial statements based on our audit. We did not audit the financial statements of Comunidad del Retiro, which represents three percent and two percent, respectively, of the assets and revenues of the aggregate remaining fund information. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for Comunidad del Retiro, is based solely on the report of other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of San Juan, Capital City of 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.

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

Our audit was conducted for the purpose of forming an opinion on the respective financial statements that collectively comprise the Municipality's basic financial statements. The combining nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for the purposes of additional analysis, as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. This supplementary information is the responsibility of Municipality's management. The combining nonmajor fund financial statements and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 6, 2006, on our consideration of Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Deloitte & Touche LLP

February 6, 2006

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**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

**Management's Discussion and Analysis
As of and for the Year Ended June 30, 2005**

The Management of the Municipality of San Juan (the "Municipality") provides the Municipality's annual financial report and the discussion and analysis of the Municipality's financial performance during the fiscal years ended June 30, 2005.

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

FINANCIAL HIGHLIGHTS

- The Municipality's net assets decreased approximately \$8.9 million.
- In the fund financial statements, total revenue increased approximately \$11.8 million (or 2.03%) while total expenditures decreased approximately \$3.5 million (or 0.53%).
- The General Fund (the primary operating fund) reflected, on a current financial resource basis, an increase of deficit of approximately \$9.3 million.
- On a budgetary basis, the General Fund's actual expenditures exceeded actual revenues by approximately \$10.6 million.
- The Municipality issued bonds and notes amounting to approximately \$31 million to finance capital improvements and equipment.

USING THIS ANNUAL FINANCIAL REPORT

This discussion and analysis is required supplementary information to the basic financial statements and is intended to serve as introduction to the basic financial statements of the Municipality. The basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains required supplementary information (budgetary schedules) and additional supplementary information (combining financial statements) in addition to the basic financial statements themselves.

Government-Wide Financial Statements

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

The Statement of Net Assets presents information on all of the Municipality's assets and liabilities, and their difference reported as net assets. Fluctuations in net assets may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

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

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Fund Financial Statements

The fund financial statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only governmental funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near term inflows and outflows of expendable resources, as well as on balances of expendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

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

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide financial statements and the fund financial statements.

Additional Supplementary Information

The basic financial statements are followed by a section of required supplementary information. This section includes a budgetary comparison schedule, which includes a reconciliation between the statutory fund balance for budgetary purposes and the fund balance for the General Fund as presented in the governmental fund financial statements.

Additional Supplementary Information

The combining financial statements referred to earlier in connection with nonmajor component units are present following the required supplementary information. The total columns of these combining financial statements carry forward to the applicable fund financial statement.

Infrastructure Assets

Historically, a government's largest group of assets (infrastructure – roads, bridges, traffic signals, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in governmental financial statements. Governmental Accounting Standards Board ("GASB") Statement No. 34 requires that these assets be valued and reported within the governmental column of the government-wide financial statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach) which periodically (at least every third year), by

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category, measures and demonstrates its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of the government infrastructure assets should assist financial statements users in evaluating a local government and its performance over time.

As of July 1, 2001, the Municipality commenced the prospective reporting of infrastructure assets. Also, the Municipality elected to depreciate infrastructure assets instead of using the modified approach.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

Condensed net asset information is presented below:

**Condensed Statements of Net Assets
As of June 30, 2005 and 2004**

	2005	2004	Change	Pctg.
ASSETS				
Capital assets	\$ 536,489,629	\$ 529,336,672	\$ 7,152,957	1%
Other assets	351,452,865	345,257,505	6,195,360	2%
Total assets	887,942,494	874,594,177	13,348,317	2%
LIABILITIES				
Current liabilities	292,478,901	272,499,512	19,979,389	7%
Noncurrent liabilities	570,090,117	567,853,294	2,236,823	0%
Total liabilities	862,569,018	840,352,806	22,216,212	3%
NET ASSETS				
Invested in capital assets, net of related debt	207,467,903	215,923,978	(8,456,075)	-4%
Restricted for:				
Debt service	9,174,521	8,906,766	267,755	3%
Capital projects	75,484,926	62,622,368	12,862,558	21%
Unrestricted	(266,753,874)	(253,211,741)	(13,542,133)	5%
Total net assets	\$ 25,373,476	\$ 34,241,371	\$ (8,867,895)	-26%

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**Management's Discussion and Analysis
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Net assets of the Municipality decreased approximately by \$8.9 million. Such decrease is the effect of the approximately \$13.3 million increase in total assets and an increase of approximately \$22.2 million in total liabilities. Total assets increased as the result of the net effect of: (i) an increase in capital assets of approximately \$7.1 million mainly due to buildings and site improvements to the Municipality's facilities; (ii) an increase of approximately \$6.2 million in other assets mainly due to an increase in intergovernmental receivables.

The Municipality's combined net assets totaled approximately \$25.4 million at the end of fiscal year 2005, compared to net assets of approximately \$34.2 million at the end of the previous year.

The largest portion of the Municipality's net assets is the unrestricted deficit. This is the consequence of previous budgets which did not provide funding for incurred long-term obligations such as compensated absences, landfill closure and post-closure costs, claims and judgments and others. Historically, such obligations have been budgeted on a pay as you go basis without providing funding for their future liquidation. Consequently, the Municipality cannot draw from its existing assets to provide services to its citizens and depends on its taxing ability to continue its operations.

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

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Changes in Net Assets

The condensed changes in net assets information is presented below:

**Condensed Statements of Activities
For the Years Ended June 30, 2005 and 2004**

	2005	2004	Change	Pctg.
Program revenues:				
Charges for services	\$ 69,272,861	\$ 78,828,465	\$ (9,555,604)	-12%
Operating grants and contributions	119,609,044	118,115,714	1,493,330	1%
Capital grants and contributions	1,701,006	2,128,040	(427,034)	-20%
General revenues:				
Property taxes	242,474,497	213,470,684	29,003,813	14%
Municipal license tax	125,252,868	119,463,489	5,789,379	5%
Grants and contributions not restricted to specific programs	26,118,653	32,736,870	(6,618,217)	-20%
Interest income	2,834,672	2,917,644	(82,972)	-3%
Other	5,077,958	12,872,843	(7,794,885)	-61%
Total revenues	592,341,559	580,533,749	11,807,810	2%
Expenses:				
General government	88,431,998	93,237,721	(4,805,723)	-5%
Public safety	47,699,570	44,531,567	3,168,003	7%
Public works	60,131,135	67,485,816	(7,354,681)	-11%
Culture and recreation	20,418,258	16,412,330	4,005,928	24%
Health and welfare	266,847,420	245,857,330	20,990,090	9%
Urban development	53,464,789	52,168,184	1,296,605	2%
Economic development	29,078,967	34,249,135	(5,170,168)	-15%
Education	9,621,025	10,197,688	(576,663)	-6%
Interest on long-term debt	25,516,292	22,741,755	2,774,537	12%
Total expenses	601,209,454	586,881,526	14,327,928	2%
Change in net assets	(8,867,895)	(6,347,777)	(2,520,118)	40%
Net assets, beginning of year	34,241,371	40,589,148	(6,347,777)	-16%
Net assets, end of year	\$ 25,373,476	\$ 34,241,371	\$ (8,867,895)	-26%

The Municipality's net assets decreased by approximately \$8.9 million. Approximately 62.1 percent (57.3 percent in 2004) of the Municipality's total revenue came from taxes, while approximately 24.9 percent (26.0 percent in 2004) resulted from grants and contributions, including federal aid. Charges for services provided approximately 11.7 percent (13.6 percent in 2004) of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for health and welfare services, general government, public works and urban development.

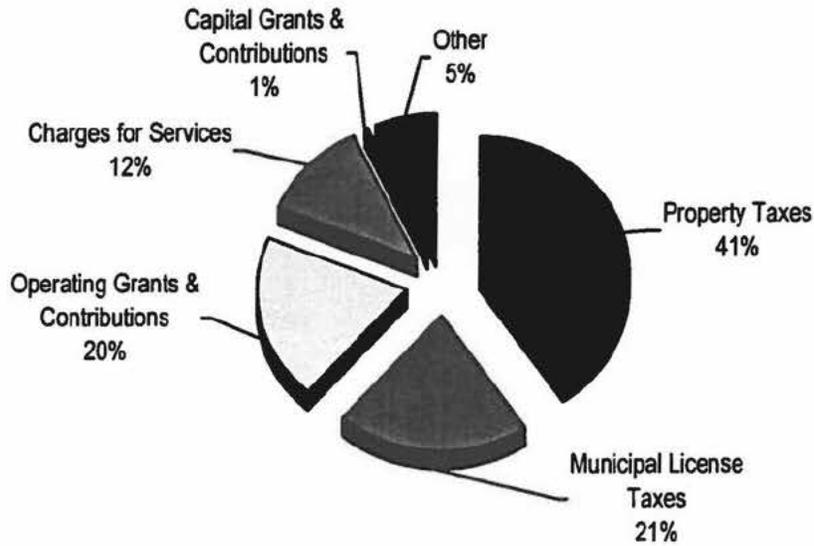
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Management's Discussion and Analysis
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Revenues from property and municipal license taxes increased by approximately 10.5 percent. Charges for services decreased by approximately 12.1 percent when compared with prior fiscal year mainly due a decrease in health care service revenues.

The following chart summarizes the Municipality revenues by sources for the governmental activities for the fiscal year ended June 30, 2005.

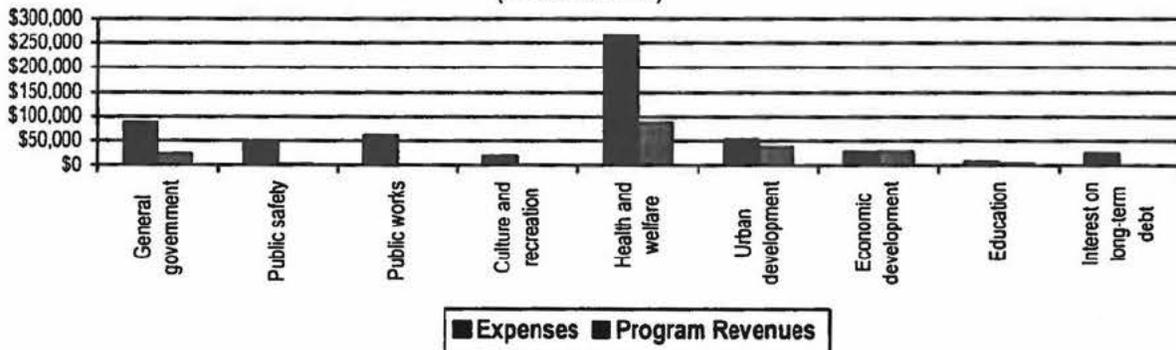
Revenues by Source-Governmental Activities



The Municipality's total expenses amounted to \$601.2 million and \$586.8 million for the year ended June 30, 2005 and 2004, respectively. Increase in total expenses was mainly due to an increase in payroll expenses and an increase in health services.

The following chart summarizes the Municipality's program revenues compared to program expenditures for the governmental activities for the fiscal year ended June 30, 2005.

Expenses and Program Revenues-Governmental Activities
(In thousands)



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FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

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

Governmental Funds

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

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$98.9 million, a decrease of \$13.9 million in comparison with the prior year. There are fund balance reserves amounting to \$115.7 million. This is the fund balance that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior fiscal year (\$24.3 million), 2) to pay debt service (\$9.2 million), 3) to pay for capital projects (\$75.5 million) or 4) for inventories not yet consumed (\$6.7 million). Accordingly, since there is an excess of reserves over the total fund balance there exists a deficiency in the unreserved balance of \$16.8 million in the governmental funds.

Within the governmental funds, it is included the general fund, which is the main operating fund of the Municipality. As of June 30, 2005 and 2004, the general fund has a deficit of \$35.2 million and \$25.9 million, respectively. Key factors in the increase of the deficit are as follows:

- Increase of \$22.2 million in total expenditures partially offset by an increase of \$14.8 million in total revenues.
- Decrease of \$10.4 million in operating transfer from the debt service fund
- Increase in other financing sources amounting \$5.9 million

There has been an increase of \$14.8 million in total revenues mainly due to an increase of \$26.1 million and \$5.8 million in property taxes and municipal license taxes, respectively, and decreases of \$8 million in license, permits and other local taxes and \$5.3 million in charges for services. The Municipality entered into an agreement (the "Agreement") with the Municipal Revenue Collection Center ("CRIM"), whereas the Municipality assumes responsibility over the property tax assessment and collections. The new Agreement allows the Municipality to extend its authority and undertake the action of collecting property taxes that are in arrears using foreclosure methods. This is the first time that CRIM enters in a comprehensive agreement with a Municipality, which is unique and represents a real opportunity to enforce a new practice that will increase property tax revenues and collections.

This foreclosure process that the Municipality is being authorized to start on CRIM's behalf is an initiative that will help the Municipality to send a message to the taxpayers, that the law will be enforced and that delinquent taxpayers will be penalized according to the applicable law. The Municipality's Legal Department has assigned a full time lawyer to assist in this process. The Municipality expects to have placed preventive liens on the identified cases by February 2006.

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The Agreement justifies the extension of the collection period for revenue recognition purposes from 60 to 360 days following June 30, 2005, as defined in National Council on Governmental Accounting ("NCGA") Interpretation 3. The effect of this extension was to increase property tax revenues by \$53.7 million. The extension of the collection period is only applicable for the year ended June 30, 2005.

Simultaneously with the implementation and enforcement of the Agreement, the Municipality has formally taken over the responsibility of property tax collections by creating and operating a Tax Adjustment and Collection Division (the "Division") within the Finance Department, dedicated exclusively to improve revenues through aggressive collection methods and to expand the taxpayers portfolio by identifying new taxpayers. San Juan is the first municipality to do this, and in view of the success that the Municipality is experimenting, the Municipality foresees that this may be a good example to other municipalities, and the Municipality could serve as the model to implement this type of unit.

The Municipality started planning, organizing, and putting together the resources for the Division since July 2005, with the assistance of a specialized consultant firm for the start up of the unit and the training of the employees. A separate office space was assigned for the Division, and necessary computer and office equipment was provided.

The Division became fully operational by September 2005. Initially ten (10) employees were identified from within the Municipality that had experience in the field. The results were quite noticeable, and soon thereafter 20 additional employees were recruited, to accelerate and expand the scope of the project. Currently, the Division has a 40-employee work force, and the Municipality expects to add 15 more employees within a month.

CRIM provided the Municipality with a portfolio of over 25,000-property tax accounts levied as of June 30, 2005, in the amount of more than \$200.0 million, which was used as the start-up agenda for the newly established Division. Collection methods include, among others, mailing of letters, visits and, receiving, orienting and assisting taxpayers at the Municipality's headquarters.

As of December 31, 2005 (3 months of operation) the following results have been accomplished:

- 7,344 collection letters were sent representing property taxes in arrears of approximately \$120.3 million.
- Collections exceeded \$4.0 million as of December 31, 2005.

Additionally, the Municipality, in conjunction with the CRIM, screened such portfolio and identified certain taxpayer accounts that are already classified as delinquent under the parameters established by CRIM regulations, whose debts will have to be collected through foreclosure methods. These identified accounts amount to \$36.2 million and have been certified as correct by the CRIM and are ready to begin with foreclosure procedures. Additional accounts in the amount of \$7.3 million are in the process of being validated by CRIM.

By following this plan, the Municipality projects to collect within a 360-day period following June 30, 2005 approximately \$60.7 million, of which approximately \$43.5 million will be collected using the foreclosure method, and approximately \$17.2 million by the reinforced collection process.

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In addition, the Municipality moved aggressively to improve the collection efforts for municipal license taxes due to a strategic plan to reduce tax evasion, better equipment and personnel training. Finally, the financial sector had a better financial performance in comparison to previous years which resulted in additional municipal license taxes revenues to the Municipality.

Furthermore, the decrease in license, permits and other local taxes was mainly due to a reduction in the construction activity on San Juan. Decrease in charges for services was related with uncovered losses on the billing system caused by the pass of Jeanne Storm.

Notwithstanding tighter controls imposed by the Municipality's management, there was an increase of \$22.2 million in expenditures mainly due to increase in salaries and increase in health services.

The increase in other financing sources amounting to \$5.9 million is the result of advances from CRIM.

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.

During the year, there was an increase of approximately \$23.4 million in appropriations between the original and final amended budget. The main component of the increase was to the Health Department for the expansion of drugs and medicines program, the increase on wages to nurse personnel and the expansion of other medical related services.

The increase was possible because of additional anticipated revenues. Those revenues included an increase in property taxes of approximately \$4 million, an increase in municipal license tax of \$2 million and the proceeds of other financing sources amounting \$17.3 million.

Notwithstanding the aggressive efforts on collections and the tighter control imposed there was a shortfall on the budget of approximately \$10.1 million.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2005 and 2004 amounted to approximately \$536.5 million and \$529.3 million, respectively, net of accumulated depreciation. This investment in capital assets includes land, buildings, sites, improvements, equipment, intangibles, infrastructure, works of art, vehicles, and construction in progress. Infrastructure assets are items that are normally immovable and of value only to the Municipality, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

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Management's Discussion and Analysis
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**Capital Assets, Net of Accumulated Depreciation (in thousands)
As of June 30, 2005 and 2004**

	2005	2004	Change	Pctg.
Land	\$ 56,551	\$ 56,551	\$ -	0%
Buildings and building improvements	212,466	225,211	(12,745)	-6%
Site improvements	97,890	108,442	(10,552)	-10%
Infrastructure	40,804	45,479	(4,675)	-10%
Equipment	6,712	8,436	(1,724)	-20%
Works of art	2,872	3,520	(648)	-18%
Intangible	1,913	2,295	(382)	-17%
Vehicles	2,420	2,716	(296)	-11%
Construction in progres	114,862	76,687	38,175	50%
Total	\$ 536,490	\$ 529,337	\$ 7,153	1%

The total increase in the Municipality's investment in capital assets was about one percent over last year. Actual expenditures to purchase or construct capital assets for the years ended June 30, 2005 and 2004 were \$42.3 and \$54.6 million, respectively. Depreciation charges amounted to \$31.3 million and \$22.3 million for the years ended June 30, 2005 and 2004, respectively.

The Municipality finances a significant portion of its construction activities through bond issuances. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2005 and 2004, the Municipality has approximately \$75.5 million and \$62.6 million, respectively, of unexpended proceeds from bond issuances that are committed to future construction activities. Additional details regarding the Municipality's capital assets can be found in the notes to the financial statements.

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.

Based on the current total net assessed valuation of real and personal property in San Juan provided by the Governmental Development Bank for Puerto Rico ("GDB") of approximately \$4.12 billion, the legal margin of San Juan as of June 30, 2005, was \$412 million. The Municipality's available legal margin as of June 30, 2005, was calculated by GDB to equal \$83.5 million after subtracting from the legal margin the amount of \$369.9 million in outstanding general obligation debt as of June 30, 2005, and adding to the legal margin the amount in its Debt Service Fund of \$41.2 million as of June 30, 2005.

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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 of July 3, 1996, as amended, provides that a municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Debt Service 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 rating assigned is BBB+, negative watch A2, by Standard & Poor's Investor Services.

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 Debt Service 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.

During fiscal year 2005, the Municipality issued bonds amounting to \$31,010,000 to provide for the construction and equipment needs of the Municipality and a refunding bond and note amounting to \$22,180,000 and \$40,033,000, respectively, to refinance old debt. At June 30, 2005, the Municipality had \$369,945,000 of general obligation bonds outstanding.

The following chart indicates the principal amortization of the Municipality's general obligation bonds in five-year increments.

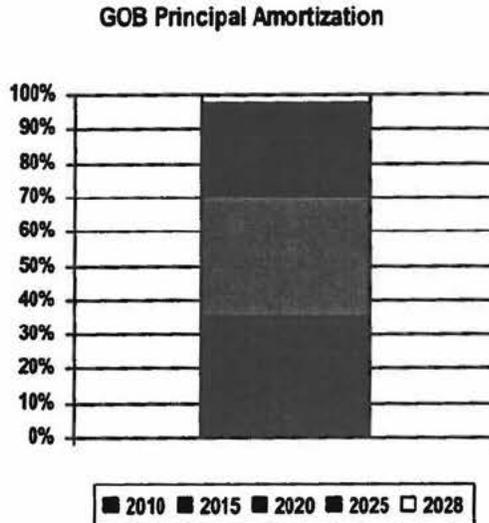
**General Obligation Bonds
Principal Amortization
In Five Year Increments Following Fiscal Year 2005**

<u>Fiscal Years</u>	<u>Principal Amortization</u>
2006-2010	\$ 129,885,000
2011-2015	131,345,000
2016-2020	66,985,000
2021-2025	32,830,000
2026-2028	8,900,000
Total	<u>\$369,945,000</u>

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Management's Discussion and Analysis
As of and for the Year Ended June 30, 2005

As can be seen in the chart below, approximately 71% of the Municipality's outstanding general obligation bonds will be retired within the next ten years.



Additional details regarding the Municipality's long-term debt can be found in the notes to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

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

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayers, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Finance Director on the 5th floor of the Municipal Tower, 160 Chardón Avenue, San Juan, Puerto Rico 00919.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO
STATEMENT OF NET ASSETS
As of June 30, 2005**

	<u>Governmental Activities</u>
<u>Assets</u>	
Cash and cash equivalents	\$ 68,542,698
Cash with fiscal agent	128,393,808
Certificate of deposit	20,062,500
Accounts receivable:	
Municipal license tax	4,000,000
Intergovernmental	106,332,421
Other	11,481,426
Inventories	6,741,795
Deferred charges	2,096,756
Restricted assets - Cash and cash equivalents	3,801,461
Capital assets not being depreciated	171,412,753
Capital assets being depreciated, net	365,076,876
	\$ 887,942,494
<u>Liabilities</u>	
Accounts payable and accrued liabilities	\$ 91,324,442
Deferred revenues:	
Municipal license tax	109,167,848
Federal grant revenues	13,133,605
Matured bonds and interest payable	36,812,868
Noncurrent liabilities:	
Due within one year	42,040,138
Due in more than one year	570,090,117
	862,569,018
<u>Net Assets</u>	
Invested in capital assets, net of related debt	207,467,903
Restricted for:	
Debt service	9,174,521
Capital projects	75,484,926
Unrestricted	(266,753,874)
	\$ 25,373,476

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

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO
STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2005**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets Governmental Activities
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
General government	\$ 88,431,998	\$ 23,225,245	\$ 45,150	\$ 1,132,869	\$ (64,028,734)
Public safety	47,699,570	309,015	3,608,495	-	(43,782,060)
Public works	60,131,135	-	-	-	(60,131,135)
Culture and recreation	20,418,258	350,585	-	-	(20,067,673)
Health and welfare	266,847,420	39,142,387	49,199,070	568,137	(177,937,826)
Urban development	53,464,789	-	38,221,482	-	(15,243,307)
Economic development	29,078,967	4,135,593	25,417,304	-	473,930
Education	9,621,025	2,110,036	3,117,543	-	(4,393,446)
Interest on long-term debt	25,516,292	-	-	-	(25,516,292)
Total governmental activities	\$ 601,209,454	\$ 69,272,861	\$ 119,609,044	\$ 1,701,006	\$ (410,626,543)

General revenues:	
Property taxes	\$ 242,474,497
Municipal license tax	125,252,868
Grants and contributions not restricted to specific programs	26,118,653
Interest income	2,834,672
Other	5,077,958
Total general revenues	401,758,648
Change in net assets	(8,867,895)
Net assets at beginning of year	34,241,371
Net assets at end of year	\$ 25,373,476

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

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

**BALANCE SHEET
GOVERNMENTAL FUNDS
As of June 30, 2005**

ASSETS	General	Debt Service Fund	Loan Guarantees Fund	Other Governmental Funds	Total Governmental Funds
Cash and cash equivalents	\$ 1,963,817	\$ -	\$ 48,058,080	\$ 18,520,801	\$ 68,542,698
Cash with fiscal agent	2,868,855	41,239,287	-	84,285,666	128,393,808
Certificate of deposit	20,062,500	-	-	-	20,062,500
Accounts receivable:					
Municipal license tax	4,000,000	-	-	-	4,000,000
Intergovernmental	82,899,703	12,962,339	-	10,470,379	106,332,421
Other	11,084,127	-	-	397,299	11,481,426
Due from other funds	19,202,592	-	-	-	19,202,592
Inventories	4,392,701	-	-	2,349,094	6,741,795
Restricted assets - cash and cash equivalents	-	-	-	3,801,461	3,801,461
Total assets	\$ 146,474,295	\$ 54,201,626	\$ 48,058,080	\$ 119,824,700	\$ 368,558,701
LIABILITIES AND FUND BALANCES (DEFICIT)					
Liabilities:					
Accounts payable and accrued liabilities	\$ 72,509,764	\$ 115,974	\$ 2,086,037	\$ 16,612,667	\$ 91,324,442
Due to other funds	-	8,098,263	586,753	10,517,576	19,202,592
Matured bonds and interest payable	-	36,812,868	-	-	36,812,868
Deferred revenues:					
Municipal license tax	109,167,848	-	-	-	109,167,848
Federal grant revenues	1,092	-	-	13,132,513	13,133,605
Total liabilities	181,678,704	45,027,105	2,672,790	40,262,756	269,641,355
Fund balances (deficit):					
Reserved for:					
Inventories	4,392,701	-	-	2,349,094	6,741,795
Debt service	-	9,174,521	-	-	9,174,521
Capital projects	-	-	-	75,484,926	75,484,926
Encumbrances	24,295,276	-	-	-	24,295,276
Unreserved:					
General fund	(63,892,386)	-	-	-	(63,892,386)
Special revenue funds	-	-	45,385,290	1,727,924	47,113,214
Total fund balances (deficit)	(35,204,409)	9,174,521	45,385,290	79,561,944	98,917,346
Total liabilities and fund balances (deficit)	\$ 146,474,295	\$ 54,201,626	\$ 48,058,080	\$ 119,824,700	

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

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	536,489,629
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the funds.	2,096,756
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the funds	(612,130,255)

Total net assets of governmental activities **\$ 25,373,476**

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

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES (DEFICIT)
GOVERNMENTAL FUNDS
For the Year Ended June 30, 2005**

	General	Debt Service Fund	Loan Guarantee Fund	Other Governmental Funds	Total Governmental Funds
REVENUES:					
Property taxes	\$ 195,436,556	\$ 47,037,941	\$ -	\$ -	\$ 242,474,497
Municipal license tax	125,252,868	-	-	-	125,252,868
Licenses, permits and other local taxes	17,264,410	-	-	-	17,264,410
Charges for services	44,303,208	-	-	1,922,886	46,226,094
Fines and forfeitures	5,782,357	-	-	-	5,782,357
Interest	2,764,763	-	27,823	42,086	2,834,672
Intergovernmental:					
Federal	-	-	-	119,609,044	119,609,044
Local	26,118,653	-	-	1,701,006	27,819,659
Other	4,349,662	-	28,425	699,871	5,077,958
Total revenues	421,272,477	47,037,941	56,248	123,974,893	592,341,559
EXPENDITURES:					
Current:					
General government	97,000,716	-	-	3,873,231	100,873,947
Public safety	45,004,472	-	-	4,409,802	49,414,274
Public works	57,195,958	-	-	644,532	57,840,490
Culture and recreation	9,728,191	-	-	2,853,255	12,581,446
Health and welfare	200,659,140	-	-	51,950,186	252,609,326
Urban development	5,912,519	-	-	44,440,132	50,352,651
Economic development	12,455,476	-	-	10,705,012	23,160,488
Education	6,192,359	-	-	3,179,940	9,372,299
Capital outlays	7,417,715	-	14,859,915	20,008,938	42,286,568
Debt service:					
Principal	10,350,679	26,630,000	-	204,978	37,185,657
Interest and other charges	1,853,052	20,140,186	-	3,523,054	25,516,292
Total expenditures	453,770,277	46,770,186	14,859,915	145,793,060	661,193,438
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(32,497,800)	267,755	(14,803,667)	(21,818,167)	(68,851,879)
OTHER FINANCING SOURCES (USES):					
Bonds issued	-	-	-	31,010,000	31,010,000
Refunding bonds issued	-	-	-	22,180,000	22,180,000
Note payable issued	17,253,000	-	-	-	17,253,000
Refunding note issued	40,033,000	-	-	-	40,033,000
Capital leases	-	-	-	593,906	593,906
Payment to refunded bond	(39,890,000)	-	-	(22,075,000)	(61,965,000)
Advances from CRIM	5,833,590	-	-	-	5,833,590
Total other financing sources (uses)	23,229,590	-	-	31,708,906	54,938,496
NET CHANGE IN FUND BALANCES (DEFICIT)	(9,268,210)	267,755	(14,803,667)	9,890,739	(13,913,383)
FUND BALANCES (DEFICIT), BEGINNING OF YEAR	(25,936,199)	8,906,766	60,188,957	69,671,205	112,830,729
FUND BALANCES (DEFICIT), END OF YEAR	\$ (35,204,409)	\$ 9,174,521	\$ 45,385,290	\$ 79,561,944	\$ 98,917,346

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

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

**RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES (DEFICIT) OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the Year Ended June 30, 2005**

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

Net change in fund balances - total governmental funds		\$ (13,913,383)
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.		
Expenditures for capital assets	\$ 42,286,568	
Loss on disposition of capital assets	(3,821,056)	
Current year depreciation	<u>(31,312,554)</u>	7,152,958

The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transactions, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities.

Bond, note and capital lease proceeds	(111,069,906)	
Advances from CRIM	(5,833,590)	
Bond issue costs	394,799	
Principal repayments	<u>99,150,657</u>	(17,358,040)

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

Amortization of deferred charges		(311,557)
Change in compensated absences accrual		(3,006,712)
Change in landfill obligation		1,718,490
Change in other liabilities		<u>16,850,349</u>
Change in net assets of governmental activities		<u>\$ (8,867,895)</u>

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

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

1. Organization and Summary of Significant Accounting Policies

The Municipality of San Juan (the "Municipality") was founded in 1521 and is the largest municipality and the Capital City of the Commonwealth of Puerto Rico. The Municipality's governmental system consists of an executive and legislature body. The Municipality is governed by a Mayor and a seventeen-member Municipal Legislature who are elected for four-year terms.

The Municipality provides public safety, public works, culture and recreation, health and welfare, urban development, education, economic development, and other miscellaneous services to its citizens.

The Municipality implemented Governmental Accounting Standards Board ("GASB") Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus – an amendment of GASB Statements No. 21 and No. 34*, GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, and GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statement*, as of July 1, 2001.

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 GASB Statement No. 14, *The Financial Reporting Entity*, as amended by GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. 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 government appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. Accounting principles generally accepted in the United States of America ("USGAAP") details two methods of presentation: (1) blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions, or (2) discrete presentation of the component units' financial data in columns separate from the Municipality's balances and transactions. The Comunidad del Retiro (the "Project") is included in the financial statements as a blended component unit.

The Project was formed for the purpose of operating 356-unit housing project for the elderly and/or handicapped. The Project is operated under Section 231 of the National Housing Act, as amended, and regulated by the U.S. Department of Housing and Urban Development as to rent charges and operating methods. Legal title of the Project is held by the Municipality.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

Separate financial statements of the individual component unit can be obtained from the Project's administrative office.

Administrative office:

Condominio Centro de Altamira
Paseo 501 Street, Suite 210
Urbanización Altamira
San Juan, Puerto Rico 00920

B. Government-wide and fund financial statements

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

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 activities of the Municipality and its component unit. 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 eliminated from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

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, charges for services and other.

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. Principal and interest due on July 1 of the following fiscal year are accounted for as a fund liability, if resources are available as of June 30 for its payment.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

Loan Guarantee Fund – is the accounting entity used to account for the loan agreement with the US Department of Housing and Urban Development under a variable rate note guaranteed pursuant to Section 108 of the Housing and Community Development Act of 1974, as amended.

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.

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 balance, revenues, and expenditures. Fund types are as follows:

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

Special Revenue Funds – Special Revenue Funds are used to account for revenues derived from 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.

Debt Service Funds – Debt Service Funds are used to account for the accumulation of resources for and the payment of long-term general obligation bonds principal, interest, and related costs.

Capital Projects Funds - Capital Projects Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

D. Measurement focus, basis of accounting, and financial statement presentation

Except for budgetary purposes, the basis of accounting used by the Municipality conforms with USGAAP as applicable to governmental units. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

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 providers have been met.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

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 expenditures in governmental funds. Proceeds from issuance of general long-term debt are reported as other financing sources.

Property taxes are considered susceptible to accrual if commonly collected within 60 days following the end of the fiscal period, unless unusual circumstances justify a greater period as defined in NCGA Interpretation 3. The Municipality understands that the unusual criteria was met through the Agreement reached with CRIM, whereas the Municipality assumes responsibility over the property tax assessment and collections, including the foreclosure process of delinquent accounts, previously done exclusively by CRIM. This agreement justifies the extension of the collection period for revenue recognition purposes from 60 to 360 days following June 30, 2005 as defined in NCGA Interpretation 3. The effect of this extension was to increase property tax revenues by \$53.7 million. The extension of the collection period is only applicable for the year ended June 30, 2005. The Municipality will continue with the collection period of 60 days beginning in fiscal year 2005-06 unless other unusual circumstances arise.

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

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.

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

The preparation of financial statements in conformity with USGAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported 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.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

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

2. *Certificate of deposit:*

The Municipality's investment policy is to minimize credit and market risk while maintaining a competitive yield on its portfolio. The Municipality is authorized under Puerto Rico's law to invest in direct obligations or obligations guaranteed by the United States government or the Commonwealth of Puerto Rico, bank acceptances, other bank obligations and certificates of deposit in financial institutions authorized to do business under the United States and Commonwealth laws. The certificate of deposit is a nonparticipating interest-earning investment contract with maturity of less than one year and is reported at cost.

3. *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 determined based upon past collection experience and current economic conditions. Intergovernmental receivables in the general fund represent mostly property tax accounts that are levied by CRIM and contributions from the Puerto Rico Electric Power Authority ("PREPA"), which contributes a specific percentage of its revenues as payment in lieu of taxes. Intergovernmental receivables in the other governmental funds represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs and the amount in the debt service fund represents the distribution of property tax collected by the CRIM, which is restricted for the debt service.

4. *Inventories:*

Inventories in the general fund are stated at cost. Inventories consist of supplies held for consumption and medicines used in providing health care services. Inventories are recorded as expenditures at the time the inventory items are consumed. A fund balance reserve equal to the value of the inventories is established in the general fund and in other governmental funds to indicate that the inventories do not constitute expendable financial resources available for appropriation.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

5. *Capital assets:*

Capital assets, which include property, plant, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the government-wide financial statements. The Municipality defines capital assets as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. 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, as well as the component unit, are depreciated using the straight-line method over the following estimated useful lives:

<u>Description</u>	<u>Years</u>
Buildings	40
Infrastructure	40
Building and site improvements	15
Works of art	10
Intangible assets	10
Vehicles	5
Equipment	3 to 5

Intangible assets at June 30, 2005, consist primarily of computer software.

6. *Long-term obligations:*

The liabilities reported in the government-wide financial statements include the general and special obligation bonds, long-term notes, other long-term liabilities, such as vacation, sick leave, claims and judgments, long-term liabilities to other governmental entities and third parties, and landfill postclosure care costs. Bond issuance costs are reported in the government-wide financial statements as deferred charges and amortized over the term of the related debt using the straight-line method.

In the fund financial statements, governmental fund types recognize bond issuance costs 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 in the general fund.

7. *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.

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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.

8. *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 when the liability is incurred.

9. *Reservations of fund balance:*

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

- a. *Inventories* - Represent fund assets that do not represent available financial resources.
- b. *Debt Service Fund* - Represents net assets available to finance future debt service payments.
- c. *Capital Projects* - Represent the reservation of amounts to be used for future expenditures of capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
- d. *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.

10. *Interfund and intra-entity transactions:*

The Municipality has the following types of transactions among funds:

- a. *Transfers* - Legally required transfers that are reported when incurred as "Transfers-in" by the recipient fund and as "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.

11. *Risk financing:*

The Municipality carries commercial insurance to cover property and 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 CRIM for the year ended June 30, 2005 amounted to approximately \$11 million. The current insurance policies have not been cancelled or terminated. CRIM also deducted approximately \$8.3 million for workers compensation insurance covering all municipal employees for the year ended June 30, 2005.

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12. Direct charges:

Pursuant to and determined by an internal cost allocation plan certain costs initially borne by the General Fund are then billed as direct charges to other funds of the Municipality. Revenues from these charges are accounted for in the government-wide Statement of Activities as general government and in the Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit) as charges for services in the general fund. The corresponding expenses appear as function/program costs in the Statement of Activities.

13. Future adoption of accounting pronouncements:

The GASB has issued the following statements that have effective dates after June 30, 2005:

- a. GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, which is effective for periods beginning after December 15, 2004.
- b. GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which is effective for fiscal years beginning after December 15, 2005.
- c. GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section – an amendment of NCGA Statement 1*, which is effective for fiscal years beginning after June 15, 2005.
- d. GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefit Other Than Pension Plans*, which is effective for periods beginning after December 15, 2006.
- e. GASB Statement No. 46, *Net Assets Restricted by Enabling Legislation, an amendment of GASB Statement No. 34*, which is effective for periods beginning after June 15, 2005.
- f. GASB Statement No. 47, *Accounting for Termination Benefits*, which is effective for periods beginning after June 15, 2005.

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

2. Deposits

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

The Municipality's bank balances in commercial banks of approximately \$14.4 million, \$48.1 million and \$19.3 million in the general fund, the loan guarantee and other governmental funds, respectively, were fully collateralized at June 30, 2005.

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Other governmental funds' deposits with GDB at June 30, 2005 amounted to approximately \$103.5 million of which \$101.7 million are reserved principally for capital projects. Debt service fund's deposits with GDB amounted to \$41.2 million at June 30, 2005. Also, the General Fund's certificate of deposit and other deposits with GDB at June 30, 2005 amounted to approximately \$20.1 million and \$2.9 million, respectively. The Municipality's deposits with GDB at June 30, 2005 are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. Receivables

A. Municipal license Tax

The Municipality imposes 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 five working days after April 15 of each year. Entities with sales volume of \$1 million 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:

- Financial business - 1.50% of gross revenues
- Other organizations - 0.20% for annual revenues up to \$1,000,000, and 0.50% over such volume.

This tax is due in two equal installments on July 15 and January 15 of each fiscal year. A discount of 5% is allowed when full payment is made on or before five working days after April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2005. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

B. Intergovernmental Receivables

Intergovernmental receivable in the general fund consists of the amount due from CRIM and the amount due from PREPA. The amount due from CRIM represents the estimated amount of real and personal property taxes levied but not yet collected by the CRIM on behalf of the Municipality. The amount due from PREPA of approximately \$19.4 million represents the amount resulting from the revenues the Municipality is entitled to receive from PREPA in lieu of payment of taxes.

On May 2004, PREPA entered into an agreement with the Municipality, related to payments owed in lieu of taxes, whereas the cost of approximately \$8.4 million for future electric energy construction will be paid by PREPA as qualifying expenditures are incurred. As of June 30, 2005, \$2.8 million were recorded as an intergovernmental receivable in the general fund as they were incurred during the period and are qualified expenditures as per the aforementioned agreement. In October 2005, PREPA transferred the \$8.4 million to a GDB account under the name of the Municipality of San Juan. The remaining balance of approximately \$5.6 million will be recognized as revenues as qualified expenditures are incurred in future years, thus improving the financial condition of the Municipality.

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The amounts receivable from other governmental entities in the General Fund are as follows:

	Amount
Due from CRIM	\$ 60,700,000
Due from PREPA	22,199,703
Total intergovernmental receivables	\$ 82,899,703

Amount presented in the debt service fund represents the special ad valorem tax restricted for debt service collected by the CRIM on behalf of the Municipality during 2005.

Intergovernmental receivables in other governmental funds represent principally expenditures incurred through the assignment of federal grants or awards not yet reimbursed by the federal and local government. Following is a detail of the intergovernmental receivable:

Description	Amount
HIV Emergency Relief Formula Grant	\$ 2,121,344
Community Services Block Grant	1,452,402
Community Development Block Grant	1,034,031
Workforce Investment Act	965,026
Housing Opportunities for Persons with AIDS	777,753
Citizen Participation	568,137
Public Safety Partnerships and Community Policing Grants	473,787
Cancer Control	412,962
Supportive Housing Program	371,461
State Federal Justice	368,646
Federal Transit Capital Improvements	344,220
Risk Reduction	321,846
Special Program for Aging – Tittle III	202,116
Emergency Shelter Grants	156,036
San Juan Shelter Plus Care Project	146,428
Corporation for National Services	145,993
Grant Resistance Education & Training	104,665
Others	503,526
Total	\$ 10,470,379

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Other

Other accounts receivable as of June 30, 2005 are as follows:

	<u>General Fund</u>	<u>Other Governmental Funds</u>	<u>Total</u>
Medical plans	\$ 5,044,240	\$ -	\$ 5,044,240
Construction permits	2,678,884	-	2,678,884
Medicare Title XVIII	1,082,293	-	1,082,293
Rent	1,062,867	-	1,062,867
Interests	542,066	-	542,066
Other	<u>673,777</u>	<u>397,299</u>	<u>1,071,076</u>
Total other receivables	<u>\$ 11,084,127</u>	<u>\$ 397,299</u>	<u>\$ 11,481,426</u>

4. Interfund Transactions

Interfund receivables and payables at June 30, 2005 are summarized as follows:

A. Due from/to other fund

<u>Receivable Fund</u>	<u>Payable Fund</u>			<u>Total</u>
	<u>Debt Service Fund</u>	<u>Loan Guarantee Fund</u>	<u>Other Governmental Funds</u>	
General	<u>\$8,098,263</u>	<u>\$586,753</u>	<u>\$10,517,576</u>	<u>\$19,202,592</u>

1. *Debt Service Fund:*

Act. No. 64 of 1996, as amended, authorized municipalities to withdraw the excess of ad valorem taxes over the actual debt service requirement. As of June 30 2005, there were approximately \$8.1 million of such excess as due from other funds in the general fund.

2. *Other Governmental Funds:*

The Municipality handles all disbursements through the general fund bank accounts. Accordingly, the amount due from other governmental funds mainly represents disbursements made on behalf of Federal Grants and Awards accounted for in other governmental funds that are reimbursed to the general fund within approximately 90-day period after year-end.

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5. Capital Assets

Capital assets are primarily funded through the issuance of long-term bonds and notes. Capital assets activity for the year ended June 30, 2005 was as follows:

Governmental Activities:	Balance July 1, 2004	Reclassifications	Additions	Retirements	Balance June 30, 2005
Capital assets, not being depreciated:					
Land	\$ 56,550,722	\$ -	\$ -	\$ -	\$ 56,550,722
Construction in progress	76,687,224	(131,639)	38,614,880	(308,434)	114,862,031
Total capital assets not being depreciated	133,237,946	(131,639)	38,614,880	(308,434)	171,412,753
Capital assets, being depreciated:					
Buildings and building improvements	300,384,179	128,389	-	(178,329)	300,334,239
Site improvements	151,222,755	9,450	-	(2,245,424)	148,986,781
Infrastructure	70,890,924	(6,200)	-	-	70,884,724
Equipment	40,270,992	-	2,266,903	(4,422,709)	38,115,186
Works of art	5,492,999	-	-	-	5,492,999
Intangible	3,825,426	-	-	-	3,825,426
Vehicles	33,418,166	-	1,404,784	(811,325)	34,011,625
Total capital assets being depreciated	605,505,441	131,639	3,671,687	(7,657,787)	601,650,980
Less accumulated depreciation for:					
Buildings and building improvements	(75,173,070)	-	(12,694,625)	-	(87,867,695)
Site improvements	(42,781,122)	-	(8,316,107)	-	(51,097,229)
Infrastructure	(25,412,339)	-	(4,668,340)	-	(30,080,679)
Equipment	(31,835,086)	-	(3,048,713)	3,481,101	(31,402,698)
Works of art	(1,972,582)	-	(648,086)	-	(2,620,668)
Intangible	(1,530,172)	-	(382,543)	-	(1,912,715)
Vehicles	(30,702,344)	-	(1,554,140)	664,064	(31,592,420)
Total accumulated depreciation	(209,406,715)	-	(31,312,554)	4,145,165	(236,574,104)
Total capital assets being depreciated, net	396,098,726	131,639	(27,640,867)	(3,512,622)	365,076,876
Governmental activities capital assets, net	\$ 529,336,672	\$ -	\$ 10,974,013	\$ (3,821,056)	\$ 536,489,629

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

<u>Governmental activities:</u>	<u>Amount</u>
General government	\$ 3,394,180
Public safety	1,622,153
Public works	2,215,369
Culture and recreation	7,107,131
Health and welfare	6,245,417
Urban development	5,198,065
Economic development	5,354,194
Education	176,045
 Total depreciation expense – governmental activities	 <u>\$ 31,312,554</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 CRIM, a governmental entity created by the Commonwealth of Puerto Rico. 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 collected for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts 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 liability to the CRIM is recorded at June 30. The difference between the preliminary and the final settlement from CRIM for fiscal year 2005 resulted in a liability of approximately \$5.8 million.

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 Law No. 83 of August 30, 1991, as amended, the exempt amount to be paid by the Puerto Rico Treasury Department to the Municipalities was frozen as of January 1, 1992. In

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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 for fiscal year 2005 is 9.03% for real property and 7.03% 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 Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected. The remaining percentage is distributed as follows: (a) 6.0% and 4.0%, respectively, represents the Municipality's basic property tax rate, which is appropriated for general purposes 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) 2.00% represents the special ad valorem tax restricted for debt service and accounted for in the debt service fund.

7. Deferred Revenues

A. Municipal License Tax

The deferred revenues of approximately \$109.2 million in the general fund at June 30, 2005 relates to municipal license tax collected in fiscal year 2005 that will be earned in fiscal year 2006.

B. Federal Government

The deferred revenues presented in other governmental funds represent 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 Vouchers	\$ 4,679,927
Welfare to Work Grants to States and Localities	2,177,524
WESTAT	2,129,076
HOME	915,636
Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation	627,385
Childhood Immunization Grants	596,174
Child and Adult Care Food Program	592,318
Law Enforcement Block Grant	489,792
Higher Education Institutional Aid - Title V	243,334
Maternal Child and Health Services Block Grant	232,668
Retired Volunteers Block Program	138,149
Department of Treasury Equitable Sharing	132,564
Others	177,966
Total	<u>\$13,132,513</u>

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8. Long-Term Debt

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

	<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	\$ 365,460,000	\$ 53,190,000	\$ (48,705,000)	\$ 369,945,000	\$ 26,325,000
Mortgage payable	5,712,779	-	(204,978)	5,507,801	223,097
Notes payable	114,725,000	57,286,000	(44,150,522)	127,860,478	4,922,801
Advances from CRIM	37,812,890	5,833,590	(3,141,062)	40,505,418	3,164,505
Obligations under capital leases	6,875,795	593,906	(2,949,094)	4,520,607	1,504,680
Compensated absences	36,184,184	7,084,927	(4,078,215)	39,190,896	2,500,000
Claims and judgments	3,000,000	1,000,000	(1,000,000)	3,000,000	1,000,000
Landfill obligation	21,718,490	-	(1,718,490)	20,000,000	800,000
Other liabilities	18,450,404	-	(16,850,349)	1,600,055	1,600,055
Total	\$ 609,939,542	\$ 124,988,423	\$ (122,797,710)	\$ 612,130,255	\$ 42,040,138

A. 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 the balance of the special ad valorem taxes in the debt service fund. In addition, before any new bonds are issued, the revenues of the debt service fund should be sufficient to cover the projected debt service requirement. Total property assessed value at June 30, 2005 amounted to approximately \$4.12 billion. Long-term debt, except for the bonds payable, is paid with unrestricted funds.

B. Bonds Payable

The Municipality issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities. During fiscal year 2005, the Municipality issued bonds for approximately \$31 million. In addition, the Municipality issued a refunding bond for approximately \$22.2 million to refinance certain debts accrued at June 30, 2004. Bonds payable outstanding at June 30, 2005 are as follows:

<u>Description</u>	<u>Outstanding Amount</u>
2004 general obligation bonds due in annual installments of \$570,000 to \$1,450,000, through July 1, 2024; with interest ranging from 4.17% to 5.28%	\$18,375,000
2004 serial bonds due in annual installments of \$365,000 to \$445,000, through July 1, 2009; with interest ranging from 4.17% to 4.38%	1,650,000
2004 general obligation bonds due in annual installments of \$500,000 to \$870,000, through July 1, 2019; with interest ranging from 3.28% to 4.80%	9,550,000

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Description	Outstanding Amount
2004 general obligation bonds due in annual installments of \$815,000 to \$1,130,000, through July 1, 2027; with interest ranging from 2.76% to 5.31%	21,365,000
2003 general obligation bonds due in annual installments of \$415,000 to \$620,000, through July 1, 2028; with interest ranging from 1.61% to 4.00%	11,990,000
2003 general obligation bonds due in annual installments of \$515,000 to \$565,000, through July 1, 2010; with interest ranging from 1.61% to 4.00%	2,740,000
2002 serial bonds due in annual installments of \$445,000 to \$590,000, through July 1, 2006; with interest ranging from 2.70% to 5.00%	590,000
2001 serial bonds due in annual installments of \$1,080,000 to \$1,475,000, through July 1, 2006; with interest ranging from 2.70% to 5.00%	1,475,000
2001 serial bonds due in annual installments of \$760,000 to \$4,825,000, through July 1, 2026; with interest ranging from 2.70% to 5.60%	52,145,000
2001 serial bonds due in annual installments of \$475,000 to \$1,195,000, through July 1, 2013; with interest ranging from 2.70% to 6.13%	7,395,000
2000 serial bonds due in annual installments of \$970,000 to \$2,680,000, through July 1, 2015; with interest ranging from 2.70% to 7.81%	19,730,000
1999 general obligations bonds due in annual installments of \$1,740,000 to \$5,885,000, through July 1, 2018; with interest ranging from 4.87% to 6.46%	52,600,000
1999 serial bonds due in annual installments of \$2,810,000 to \$7,255,000, through July 1, 2013; with interest ranging from 4.87% to 6.11%	46,335,000
1999 general obligations bonds due in annual installments of \$1,980,000 to \$6,260,000, through July 1, 2016; with interest ranging from 4.87% to 6.34%	50,190,000
1998 serial bonds due in annual installments of \$1,190,000 to \$4,695,000, through July 1, 2017; with interest ranging from 4.87% to 6.71%	39,030,000
1998 general obligations bonds due in annual installments of \$350,000 to \$1,605,000, through July 1, 2019; with interest ranging from 4.87% to 6.71%	14,605,000
1996 serial bonds due in annual installments of \$885,000 to \$2,830,000, through July 1, 2011; with interest ranging from 4.70% to 6.63%	14,125,000

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Description	Outstanding Amount
1996 general obligations bonds due in annual installments of \$420,000 to \$1,150,000, through July 1, 2009; with interest ranging from 4.87% to 6.75%	4,100,000
1987 serial bonds due in annual installments of \$485,000 to \$1,955,000, through July 1, 2006; with interest ranging from 8.20% to 9.00%	1,955,000
Total	\$369,945,000

These bonds are payable from the special ad valorem property tax of 2.00%, which is restricted for debt service and retained by GDB for such purposes.

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

Year ending June 30,	Principal	Interest
2006	\$ 26,325,000	\$ 19,183,269
2007	23,790,000	17,906,181
2008	25,400,000	16,636,180
2009	27,115,000	15,252,510
2010	27,255,000	13,794,609
2011 - 2015	131,345,000	46,215,459
2016 - 2020	66,985,000	16,602,626
2021 - 2025	32,830,000	6,079,594
2026 - 2028	8,900,000	299,450
Total	\$ 369,945,000	\$ 151,969,878

C. Mortgage Payable

The mortgage loan payable to the federal government bears interest at 8.5% and is secured by the Federal Housing Administration and by a first mortgage on rental property. Principal and interest are payable from the proceeds of the rent collected from the tenants. The Federal government provides housing assistance payments to qualified tenants to subsidize most of the monthly rent. This housing project is administered by a private entity.

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Aggregate annual maturities of the mortgage payable are as follows:

Year ending June 30,	Principal	Interest
2006	\$ 223,097	\$ 459,604
2007	242,817	439,885
2008	264,279	418,422
2009	287,639	395,062
2010	313,065	369,637
2011 - 2015	2,032,678	1,380,828
2016 - 2019	2,144,226	358,992
Total	\$ 5,507,801	\$ 3,822,430

D. Notes Payable

During November 2004, the Municipality issued a special obligation refunding note with a commercial bank for approximately \$40 million to refinance certain notes payable to GDB. The note bears interest at 90-day London Interbank Offering Rate ("LIBOR") plus 1.25% (4.37% at June 30, 2005) and is payable semi-annually, and matures at various dates through July 1, 2029. The note will be repaid through withholdings of property tax advances by CRIM.

During May 2005, the Municipality issued a note payable to GDB for approximately \$17.3 million. The note is payable in annual installments ranging from \$1.4 to \$2.1 million through July 2014 and bears interest at 1.25% over 90-day LIBOR with a minimum of 5% and maximum of 12% (5% at June 30, 2005). The proceeds of the note were used principally to pay debt incurred in prior years.

In addition, the Municipality entered into a loan agreement with the US Department of Housing and Urban Development under a variable rate note guaranteed pursuant to Section 108 of the Housing and Community Development Act of 1974, as amended. The note was issued to finance the future acquisition and construction of major capital facilities, and allows borrowings up to a maximum of \$72,515,000. There were no borrowings made during fiscal year 2005. The borrowings are payable in annual installments, mature at various dates through July 2022 and bear interest at 0.2% over 90-day LIBOR (3.32% at June 30, 2005).

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The notes are payable as follows:

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 4,922,801	\$ 6,082,515
2007	5,184,063	5,890,069
2008	5,468,007	5,671,322
2009	5,759,789	5,427,933
2010	6,079,574	5,160,984
2011 - 2015	33,459,507	20,993,411
2016 - 2020	33,485,538	12,785,801
2021 - 2025	22,757,891	4,346,593
2026 - 2029	10,743,308	1,000,930
Total	<u>\$ 127,860,478</u>	<u>\$ 67,359,558</u>

E. Advances from CRIM

This amount represents the balance owed to CRIM at June 30, 2005, from the excess of property tax advances over actual collections during fiscal years ended June 30, 1992, 1999, 2000 and 2005.

On December 31, 1992, the Municipality entered into a non-interest bearing 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 \$8.3 million.

On January 26, 2000, Public Law 42 was enacted, which authorized CRIM to obtain a loan up to \$200 million, to allow for the financing of the debt that the Municipalities of Puerto Rico have with CRIM arising from final settlements of property tax advances versus actual collections for fiscal years 1999 and 2000. The amounts that the Municipalities will collect from the additional property taxes resulting from the increases in the subsidy from the Central Government to the Municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law 238, enacted on August 15, 1999.

During September 2002, the Municipality entered into a repayment agreement with the GDB and CRIM to repay the remaining \$27.4 million of excess property tax advances from fiscal years 1999 and 2000. The CRIM will retain the principal and interest from the property tax advances. The amounts retained by CRIM will be remitted to GDB on July 1 of each year through July 1, 2032. The outstanding balance as of June 30, 2005 approximates \$26.4 million. The repayment agreement bears interest at a fixed interest rate of 6.19%.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

During the current fiscal year ended June 30, 2005, advances of property taxes exceeded the amounts actually collected by CRIM by approximately \$5.8 million. CRIM will retain such excess from the 2006-2007 property tax advances and the repayment will not bear interest.

The advances are payable as follows:

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 3,164,505	\$ 1,632,587
2007	9,022,986	1,607,694
2008	3,215,832	1,581,261
2009	481,705	1,553,192
2010	511,510	1,523,387
2011 – 2015	3,073,326	7,101,158
2016 – 2020	4,149,307	6,025,177
2021 – 2025	5,601,993	4,572,491
2026 – 2030	7,563,269	2,611,215
2031 – 2032	3,720,985	348,809
Total	<u>\$ 40,505,418</u>	<u>\$ 28,556,971</u>

F. Obligations Under Capital Leases

The Municipality has entered into various capital lease agreements to finance the acquisition of equipment mainly related to the implementation of information systems. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date. At June 30, 2005, the cost and net book value of the capitalized assets amounts to approximately \$21.2 million and \$2.8 million, respectively, and are recognized as equipment in the statement of net assets.

During July 2003, the Municipality entered into a non-revolving line of credit with a commercial bank for \$5.5 million. The line of credit matures in five years and bears interest at a fixed interest rate of 3.85%. Outstanding balance of line of credit amounted to approximately \$4.0 million at June 30, 2005. The proceeds of the line were use for the improvements to the data processing network and for the acquisition of medical equipment.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

The future minimum lease obligations and the net present value of these minimum lease payments as of June 30, 2005, were as follows:

<u>Year ending June 30,</u>	<u>Amount</u>
2006	\$ 1,637,842
2007	1,307,261
2008	1,191,072
2009	637,752
2010	<u>28,369</u>
Total minimum lease payments	4,802,296
Less amount representing interest (ranging from 1.66% to 7.40%)	<u>281,689</u>
Present value of minimum lease payments	<u>\$4,520,607</u>

G. Compensated Absences

The government-wide statement of net assets includes approximately \$21.3 million of accrued sick leave benefits, and approximately \$17.9 million of accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

H. Landfill Obligation

State and federal laws and regulations require the Municipality to place a final cover on the Municipality's landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. On December 2000, the Municipality's landfill facilities were closed. Based on current costs, the preliminary annual estimate of postclosure costs has been assessed approximately to be \$800,000 for a period of approximately 25 years. The balance of postclosure costs of \$20 million is reported in the statement of net assets. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations.

I. Other Liabilities

Other liabilities include approximately \$1.2 million accrued for possible claims arising from federal cost disallowances as a result of current and prior audits of federally financed programs, and approximately \$400,000 due to CRIM in connection with a project to establish an automated information system.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

9. Pension Plan

Employees of the Municipality participate in the Employees' Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities (the "System"). The System is cost-sharing multi-employer defined benefit pension plan sponsored by the Commonwealth of Puerto Rico under the terms of Act No. 447 of 1951, as amended. Participation is mandatory for regular employees. The System issues a publicly available financial report that includes its financial statements and required supplementary information.

Members who have attained at least 55 years of age and have completed at least 25 years of creditable service or members who have attained at least 58 years of age and have completed at least 10 years of creditable service are entitled to an annual benefit, payable monthly for life.

The amount of the annuity shall be 1.5% of the average compensation, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% 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 up to a maximum of 65% of the average compensation, as defined, or if they have attained 55 years of age will receive up to a maximum of 75% of the average compensation, as defined. Disability retirement benefits are available to members for occupational and non-occupational disability up to a maximum benefit of 50% of the average compensation, as defined. However, for non-occupational disability, a member must have at least 10 years of creditable service.

Act No. 1 of 1990 made certain amendments applicable to new participants joining the System effective April 1, 1990. These changes consist principally of the establishment of contributions at 8.275% of their monthly gross salary, an increase in the retirement age to 65, a decrease in the annuity benefit to 1.5% of the average compensation, as defined, for all years of creditable service, a decrease in the maximum disability, and death benefits annuities from 50% to 40% of average compensation, as defined, and the elimination of the Merit Annuity for participants who have completed 30 years of creditable service.

The contribution requirements for both employees and employers are established by law and are not actuarially determined. Employees are required to contribute 5.775% or 8.275% of their monthly gross salary. The Municipality is required to contribute 9.275% of its employees' gross salaries.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the System, was enacted with the purpose of establishing a new pension program (System 2000). System 2000 became effective on January 1, 2000. Employees participating in the current system as of December 31, 1999, elected either to stay in the defined-benefit plan or transfer to the new program. Persons joining the government on or after January 1, 2000, will only be allowed to become members of System 2000.

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 the System, together with those of the current defined-benefit plan. Benefits at retirement age will not be guaranteed by the Commonwealth of Puerto Rico. The annuity will be based on a formula which assumes that each year the employees' contribution (with a

**MUNICIPALITY OF SAN JUAN,
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Notes to Financial Statements
As of and for the Year Ended June 30, 2005

minimum of 8.275% of the employees' salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note; or (2) earn a rate equal to 75% of the return of the System's investment portfolio (net of management fees); or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employers' contributions (9.275% of the employees' salary) will be used to fund the current plan.

System 2000 reduces the retirement age from 65 years to 60 years for those employees who joined the current plan on or after April 1, 1990.

Funding Policy

Contribution requirements are established by law and are as follows:

Municipality	9.275% of gross salary
Employees:	
Hired on or before March 31, 1990	5.775% of gross salary up to \$6,600
	8.275% of gross salary over \$6,600
Hired on or after April 1, 1990	8.275% of gross salary

Total employee contributions to the above-mentioned plans during the year ended June 30, 2005 amounted to approximately \$11.4 million. The Municipality's contributions during the years ended June 30, 2005, 2004 and 2003 amounted to approximately \$13.1 million, \$11.3 million, and \$10.5 million, respectively. These amounts represented 100% of the required contribution for the corresponding year.

The Municipality follows the provisions of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, which requires employers that participate in cost-sharing multi-employer defined-benefit pension plans to recognize pension expenditures/expense equal to the employer's contractually required contributions and a liability for unpaid contributions.

Additional information on the System is provided in its financial statements for the year ended June 30, 2005, a copy of which can be obtained from the Employees' Retirement System of the Commonwealth of Puerto Rico and its Instrumentalities, PO Box 42003, San Juan, PR 00940-2003.

10. Risk Management

The Risk Management Division of the Municipality is responsible of assuring that the Municipality's property is properly insured. Annually, the Risk Management Division compiles the information of all property owned and its respective market value. After evaluating this information, the Risk Management Division submits the data regarding the Municipality's properties to the Area of Public Insurance at the Department of the Treasury of the Commonwealth of Puerto Rico who is responsible for purchasing all property and casualty insurance policies of all municipalities. Settled claims have not exceeded commercial coverage in any of the past three fiscal years.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

The Municipality maintained a claims-made policy since October 15, 1990 for the purpose of providing professional and patient care liability insurance with liability limits of \$300,000 for each medical incident and \$2 million for aggregate incidents. The effective date of the policy is from January 24, 2005, through January 24, 2006. The Municipality also obtained tail insurance coverage for incidents incurred but not reported prior to October 14, 1990.

11. Commitments

A. Operating Leases

The Municipality leases real property, buildings, vehicles and equipment under several operating lease agreements, which generally have terms of one year or less and are automatically renewed for the same terms. Rental expenditures recorded in the general fund and in other governmental funds for the year ended June 30, 2005, amounted to approximately \$4.7 million and \$1.8 million, respectively. Management believes that the summary of the future minimum rental commitments under noncancelable real property and equipment lease with terms exceeding one year is not significant.

B. Construction

The Municipality had commitments at June 30, 2005 of approximately \$75.7 million for the construction, improvements, or renovation of several municipal facilities.

C. Electric Energy Infrastructure

The Law No. 83 of May 1941, as amended, established that PREPA will pay a contribution to the municipalities equal to seven (7) percent of PREPA's net income in lieu of taxes. In May 2004, PREPA entered into an agreement to settle balances owed to all municipalities for previous years. As part of this agreement, PREPA paid approximately \$10 million to the Municipality during fiscal year 2004. In addition, PREPA will absorb the cost of approximately \$8.4 million for future electric energy construction of infrastructure assets, as approved by the Municipality through fiscal year 2007.

12. Contingencies

A. Losses

The Municipality is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, including medical malpractice claims from the Municipality's Department of Health.

With respect to pending and threatened litigation, the Municipality has reported liabilities of approximately \$3 million at June 30, 2005, for anticipated unfavorable judgments. These amounts were included in the financial statements and represent the amounts estimated as probable liabilities, 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 condition of the Municipality.

**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

Notes to Financial Statements
As of and for the Year Ended June 30, 2005

The Municipality participates in a number of federal financial assistance programs funded by the Federal Government. Expenditures financed by these programs are subject to financial and compliance audits by the appropriate grantor. The *"Reports on Compliance and Internal Control in Accordance with Government Auditing Standards and the Requirements of OMB Circular A-133"* for the year ended June 30, 2005, disclosed several material instances of noncompliance with applicable laws and regulations and with internal accounting and administrative controls. If expenditures are disallowed due to noncompliance with grant programs regulations, the Municipality may be required to reimburse the grantor. Management believes that the Municipality will be able to comply with the terms of corrective action plans that may be requested by the federal grantors.

B. Gains

The Municipality is a plaintiff in a number of lawsuits arising principally from claims against the Commonwealth of Puerto Rico for alleged, among others, non compliance with certain government-mandated transactions and the final settlement of property tax revenues provided by CRIM. Also, the Municipality is a plaintiff on several lawsuits from claims against taxpayers for alleged differences on computation of the municipal license tax.

With respect to pending and threatened litigation, the Municipality has not reported any receivables at June 30, 2005, for anticipated favorable judgments of approximately \$22 million. Although this amount was not included in the financial statements, the amount estimated as a probable receivable would represents future available financial resources for expenditures.

It is management's opinion, based on the advice of the legal counsel, that the potential claims against the Commonwealth of Puerto Rico and certain taxpayers will materially improve the financial condition of the Municipality.

13. Subsequent Events

During November 2005, the Municipality entered into various agreements with private investors for the sale of certain Municipal's capital assets for an efficient land use program to re-develop certain San Juan's clusters for mixed use of residential and commercial purposes. The aggregate amount for these agreements totaled approximately \$14 million. A summary of these transactions follows:

- On November 23, 2005; three parcels of land of approximately 3,683 square meters, each with a concrete structure were sold for \$2.1 million.
- On November 23, 2005; seven parcels of land of approximately 12,111 square meters with a commercial structure of approximately 47,100 square feet were sold for \$6.5 million.
- On November 25, 2005; three parcels of land of approximately 1,942 square meters were sold for \$350,000.
- On November 30, 2005; two parcels of land of approximately 8,598 square meters with a commercial structure of approximately 27,800 square feet were sold for \$5.1 million.

During November 2005, the Municipality issued a general obligation bond that amounted \$18.62 million for capital improvements. The bond will due in annual installments through July 2025 and will bear interest at 90-day LIBOR plus 1.25 percent.

In addition, the Municipality issued a general obligation note in December 2005 that amounted to approximately \$6 million for the acquisition of equipment. The note will be due in annual installments through July 2021 and will bear interest at 90-day LIBOR plus 1.25 percent.

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**MUNICIPALITY OF SAN JUAN,
CAPITAL CITY OF PUERTO RICO**

**BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
For the Year Ended June 30, 2005**

	Budgeted Amounts		Actual Amounts (Budgetary Basis) (See Note 1)	Variance with Final Budget - Positive (Negative)
	Original	Final		
REVENUES:				
Property taxes	\$ 147,506,933	\$ 151,622,416	\$ 201,270,146	\$ 49,647,730
Municipal license tax	123,600,000	125,600,000	125,252,868	(347,132)
Licenses, permits and other local taxes	25,354,000	25,354,000	17,264,410	(8,089,590)
Charges for services	47,836,100	47,839,100	44,303,208	(3,535,892)
Fines and forfeitures	4,800,000	4,800,000	5,782,357	982,357
Interest	5,500,000	5,500,000	2,764,763	(2,735,237)
Intergovernmental - local	23,244,812	23,244,812	26,118,653	2,873,841
Other	1,935,000	19,185,100	21,602,662	2,417,562
	<u>379,776,845</u>	<u>403,145,428</u>	<u>444,359,067</u>	<u>41,213,639</u>
EXPENDITURES:				
Current:				
General government	108,510,667	105,112,468	109,834,484	(4,722,016)
Public safety	38,485,729	38,832,015	46,189,922	(7,357,907)
Public works	43,832,784	46,200,757	60,629,013	(14,428,256)
Culture and recreation	8,576,149	9,488,858	11,005,969	(1,517,111)
Health and welfare	159,847,095	181,398,213	201,781,021	(20,382,808)
Urban development	6,080,628	6,125,105	6,191,718	(66,613)
Economic development	8,726,326	10,270,545	12,359,572	(2,089,027)
Education	5,717,467	5,717,467	6,495,453	(777,986)
	<u>379,776,845</u>	<u>403,145,428</u>	<u>454,487,152</u>	<u>(51,341,724)</u>
DEFICIENCY OF REVENUES OVER EXPENDITURES			<u>\$ (10,128,085)</u>	<u>\$ (10,128,085)</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis) "available for appropriation" from the budgetary comparison schedule				\$ 444,359,067
Differences - budget to GAAP:				
The proceeds from advances from CRIM are budgetary resources but are regarded as Other Financing Sources for financial reporting purposes				(5,833,590)
The proceeds from the issuance of long-term debt are budgetary resources but are regarded as Other Financing Sources for financial reporting purposes				(17,253,000)
Total revenues as reported in the statement of revenues, expenditures, and changes in fund balances (deficit) - General Fund				<u>\$ 421,272,477</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule				\$ 454,487,152
Differences - budget to GAAP:				
Prior year encumbrances recorded as current year expenditures for GAAP basis				23,578,401
Current year encumbrances recorded as expenditures for budgetary purposes				(24,295,276)
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances (deficit) - General Fund				<u>\$ 453,770,277</u>

The notes to budgetary comparison schedule are an integral part of this schedule.

**MUNICIPALITY OF SAN JUAN
CAPITAL CITY OF PUERTO RICO**

Notes to Budgetary Comparison Schedule – General Fund
For the 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 USGAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of certain appropriations within the budget, known as Mayor's Executive Orders, do not require the approval of the Municipal Legislature. The Municipality prepares its annual budget including the operations of the general fund.

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

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

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

MUNICIPALITY OF SAN JUAN,
 CAPITAL CITY OF PUERTO RICO
 Combining Balance Sheet
 Other Governmental Funds
 As of June 30, 2005

	Special Revenue Funds					Capital Project Funds			Total Other Governmental Funds	
	Department of Justice Funds	Department of Labor Funds	Health & Human Services Funds	Housing & Urban Development Funds	Miscellaneous Special Revenues Funds	Comunidad del Retiro	Joint Resolution Funds	Citizen Participation Funds		Various Bond Issue Funds
ASSETS										
Cash and cash equivalents	\$ 20,768	\$ 9,466	\$ 974,827	\$ 12,525,508	\$ 1,267,318	\$ 41,859	\$ 3,397,546	\$ 263,509	\$ -	\$ 18,520,801
Cash with fiscal agent	-	1,841,261	-	-	-	-	-	-	82,444,405	84,285,666
Accounts receivable - intergovernmental	1,108,472	965,026	4,391,063	2,566,410	871,271	-	-	568,137	-	10,470,379
Accounts receivable - other	-	3,786	132,922	106,311	38,424	115,856	-	-	-	397,299
Inventories	-	-	2,349,094	-	-	-	-	-	-	2,349,094
Restricted assets - cash and cash equivalents	-	-	-	-	-	3,801,461	-	-	-	3,801,461
Total assets	\$ 1,129,240	\$ 2,819,539	\$ 7,847,906	\$ 15,198,229	\$ 2,197,013	\$ 3,959,176	\$ 3,397,546	\$ 831,646	\$ 82,444,405	\$ 119,824,700
LIABILITIES AND FUND BALANCES (DEFICIT)										
Liabilities										
Accounts payable and accrued liabilities	\$ 180,461	\$ 90,805	\$ 532,625	\$ 3,913,589	\$ 219,290	\$ 339,624	\$ 114,208	\$ 34,898	\$ 11,187,167	\$ 16,612,667
Due to other fund	488,457	888,491	2,170,117	2,906,283	4,211,830	-	(450,765)	22,601	280,562	10,517,576
Deferred revenues	489,806	2,177,524	3,056,845	6,306,531	1,101,707	-	-	-	-	13,132,513
Total liabilities	1,158,724	3,156,820	5,759,587	13,126,503	5,532,827	339,624	(336,557)	57,499	11,467,729	40,262,756
Fund balances (deficit):										
Reserved for inventories	-	-	2,349,094	-	-	-	-	-	-	2,349,094
Reserved for capital projects	-	-	-	-	-	-	3,734,103	774,147	70,976,676	75,484,926
Unreserved in Special Revenue Funds	(29,484)	(337,281)	(260,775)	2,071,726	(3,335,814)	3,619,552	-	-	-	1,727,924
Total fund balances (deficit)	(29,484)	(337,281)	2,088,319	2,071,726	(3,335,814)	3,619,552	3,734,103	774,147	70,976,676	79,561,944
Total liabilities and fund balances (deficit)	\$ 1,129,240	\$ 2,819,539	\$ 7,847,906	\$ 15,198,229	\$ 2,197,013	\$ 3,959,176	\$ 3,397,546	\$ 831,646	\$ 82,444,405	\$ 119,824,700

MUNICIPALITY OF SAN JUAN,
 CAPITAL CITY OF PUERTO RICO
 Combining Statement of Revenues, Expenditures and Changes in Fund Balances (Deficit)
 Other Governmental Funds
 For the Year Ended June 30, 2005

	Social Revenue Funds						Capital Project Funds			Total Other Governmental Funds	
	Department of Justice Fund	Department of Labor Funds	Health & Human Services Funds	Housing & Urban Development Funds	Miscellaneous Special Revenues Funds	Comunidad del Retiro	Joint Resolution Funds	Citizen Participation Funds	Various Bond Issue Funds		
REVENUES:											
Charges for services	\$ -	\$ -	\$ -	\$ 750	\$ -	\$ 1,922,136	\$ -	\$ -	\$ -	\$ 1,922,886	1,922,886
Interest	33	295	14,237	22,761	2,090	-	2,670	-	-	42,086	42,086
Intergovernmental Federal	3,481,179	7,170,386	44,361,630	58,259,713	6,336,136	-	-	-	-	119,609,044	119,609,044
Intergovernmental Local	-	-	-	-	-	-	1,132,869	568,137	-	1,701,006	1,701,006
Other	-	-	-	649,471	50,400	-	-	-	-	699,871	699,871
Total revenues	3,481,212	7,170,681	44,375,867	58,932,695	6,388,626	1,922,136	1,135,539	568,137	-	123,974,893	123,974,893
EXPENDITURES:											
Current:											
General government	70,819	25,538	1,858,416	591,788	1,140,951	-	111,162	-	74,557	3,873,231	3,873,231
Public safety	3,461,927	251,948	-	451,400	163,970	-	7,293	-	73,264	4,409,902	4,409,902
Public works	-	-	-	13,650	-	-	15,000	-	615,882	644,532	644,532
Culture and recreation	-	5,000	-	888,971	1,517,007	-	254,149	-	188,128	2,853,255	2,853,255
Health and welfare	130,911	886	43,594,353	4,157,747	2,779,687	-	246,644	351,719	888,239	51,950,186	51,950,186
Urban development	-	-	-	41,420,375	170,390	2,007,988	175,881	200,000	465,498	44,440,132	44,440,132
Economic development	-	6,881,445	-	3,658,470	29,629	-	3,060	-	132,408	10,705,012	10,705,012
Education	-	65,607	-	-	3,114,333	-	-	-	-	3,179,940	3,179,940
Capital outlays	-	-	57,021	3,612,974	3,380	(17,671)	269,071	-	16,084,163	20,008,938	20,008,938
Debt service:											
Principal	-	-	-	-	-	204,978	-	-	-	204,978	204,978
Interest and other charges	-	-	-	3,523,054	-	-	-	-	-	3,523,054	3,523,054
Total expenditures	3,663,657	7,230,424	45,506,790	58,318,429	8,919,347	2,195,295	1,082,260	551,719	18,322,139	145,793,060	145,793,060
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(182,445)	(59,743)	(1,133,923)	614,266	(2,530,721)	(273,159)	53,279	16,418	(18,322,139)	(21,818,167)	(21,818,167)
OTHER FINANCING SOURCES:											
Bonds issued	-	-	-	-	-	-	-	-	28,995,000	28,995,000	31,010,000
Refunding bonds issued	-	-	-	-	-	-	-	-	22,180,000	22,180,000	22,180,000
Note payable issued	-	-	-	-	-	-	-	-	2,015,000	2,015,000	-
Lease agreements issued	-	-	-	-	593,906	-	-	-	-	593,906	593,906
Payment to refunded bond	-	-	-	-	-	-	-	-	(22,075,000)	(22,075,000)	(22,075,000)
Total other financing sources	-	-	-	-	593,906	-	-	-	31,115,000	31,708,906	31,708,906
NET CHANGES IN FUND BALANCES (DEFICIT)	(182,445)	(59,743)	(1,133,923)	614,266	(1,936,815)	(273,159)	53,279	16,418	12,792,861	9,890,739	9,890,739
FUND BALANCES (DEFICIT), BEGINNING YEAR	152,961	(277,538)	3,222,242	1,457,460	(1,398,999)	3,692,711	3,680,824	757,729	58,183,815	69,671,205	69,671,205
FUND BALANCES (DEFICIT), END OF YEAR	\$ (29,484)	\$ (337,281)	\$ 2,088,319	\$ 2,071,726	\$ (3,335,814)	\$ 3,619,552	\$ 3,734,103	\$ 774,147	\$ 70,976,676	\$ 79,561,944	\$ 79,561,944

MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART II

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

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

The Honorable Mayor and Members of the Municipal Legislature
Municipality of San Juan
San Juan, Puerto Rico

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Municipality of San Juan, Puerto Rico (the "Municipality"), as of and for the year ended June 30, 2005, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated February 6, 2006. We did not audit the financial statements of Comunidad del Retiro, which represents three percent and two percent, respectively, of the assets and revenues of the aggregate remaining fund information. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for Comunidad del Retiro, is based solely on the report of other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Municipality's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect the Municipality's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 05-01 to 05-06.

A material weakness is a reportable 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 caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 05-01, 05-02, 05-05, and 05-06 to be material weaknesses.

Compliance and Other Matters

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

This report is intended solely for the information and use of the Municipal Legislature, management, federal awarding agencies, state funding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLP

February 6, 2006

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MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART III

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE
AND INTERNAL CONTROL OVER COMPLIANCE
APPLICABLE TO EACH MAJOR FEDERAL AWARD PROGRAM**

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND INTERNAL CONTROL OVER COMPLIANCE APPLICABLE TO EACH MAJOR FEDERAL AWARD PROGRAM

The Honorable Mayor and Members of the Municipal Legislature
Municipality of San Juan
San Juan, Puerto Rico

Compliance

We have audited the compliance of the Municipality of San Juan, Puerto Rico (the "Municipality"), with the types of compliance requirements described in the *U.S. Office of Management and Budget ("OMB") Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2005. We did not audit the financial statements of Comunidad del Retiro, which represents three percent and two percent, respectively, of the assets and revenues of the aggregate remaining fund information. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for Comunidad del Retiro, is based solely on the report of other auditors. The Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grant agreements, applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on the Municipality's compliance 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; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Municipality's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Municipality's compliance with those requirements.

As described in the table below and discussed in detail in the accompanying Schedule of Findings and Questioned Costs listed in the Table of Contents, the Municipality did not comply with the requirements regarding allowable costs/costs principles; eligibility; equipment and real property management; earmarking; procurement and suspension and debarment; program income; reporting; subrecipient monitoring; and applicable special tests and provisions that are applicable to the following federal

programs: Section 8 Housing Choice Voucher; Lower Income Housing Assistance – Section 8 Moderate Rehabilitation; Housing Opportunities for Persons with AIDS; HOME Investment Partnership Program; HIV Emergency Relief Project Grants; Workforce Investment Act; and Head Start.

Compliance with such requirements is necessary, in our opinion, for the Municipality to comply with requirements applicable to these programs.

Compliance Requirement	Major Program	Reference Number
Allowable Costs/Cost Principles	Section 8 Housing Choice Vouchers	05-10
	Housing Opportunities for Persons with AIDS	05-26
	HOME Investment Partnership Program	05-30
Earmarking	HOME Investment Partnership Program	05-28,05-31
Eligibility	Section 8 Housing Choice Vouchers	05-11,05-12
	Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation	05-19,05-20
	HOME Investment Partnership Program	05-28,05-31
Equipment and Real Property Management	HOME Investment Partnership Program	05-29
	HIV Emergency Relief Project Grants	05-32
	Workforce Investment Act	05-34
	Head Start	05-35
Program Income	HOME Investment Partnership Program	05-27
Reporting	Section 8 Housing Choice Vouchers	05-11,05-18
	Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation	05-19,05-22,05-23
	Housing Opportunities for Persons with AIDS	05-25
	HOME Investment Partnership Program	05-27
	Workforce Investment Act	05-33
Subrecipient Monitoring	Housing Opportunities for Persons with AIDS	05-26
Special Tests and Provisions	Section 8 Housing Choice Vouchers	05-11,05-13, 05-14, 05-15, 05-16, 05-17
	Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation	05-19,05-21,05-24
	HOME Investment Partnership Program	05-31

In our opinion, except for the noncompliance described in the preceding paragraph, the Municipality complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2005.

Internal Control Over Compliance

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

opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the Municipality's internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Municipality's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grant agreements. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 05-07 to 05-35.

A material weakness is a reportable 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 grant agreements caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider items 05-07, 05-08, 05-09, 05-10, 05-11, and 05-20 to be material weaknesses.

This report is intended solely for the information and use of the Municipal Legislature, management, federal awarding agencies, state funding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Deloitte & Touche LLP

March 24, 2006

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MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART IV

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

PART I – SUMMARY OF AUDITORS' RESULTS

1. The independent auditors' report on the basic financial statements expressed an unqualified opinion.
2. Reportable conditions in internal control over financial reporting were identified, some of which are considered to be material weaknesses.
3. Instances of noncompliance considered material to the financial statements were disclosed by the audit.
4. Reportable conditions in internal control over compliance with requirements applicable to major federal award programs were identified, some of which are considered to be material weakness:
5. The independent auditors' report on compliance with requirements applicable to major federal award programs expressed a qualified opinion.
6. The audit disclosed findings required to be reported by OMB Circular A-133.
7. The Municipality's major programs were:

Name of Federal Program	CFDA Number
Section 8 Housing Choice Vouchers	14.871
Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation	14.856
Housing Opportunities for Persons with AIDS	14.241
HOME Investment Partnerships Program	14.239
Community Development Block Grants/Entitlement Grants	14.218
HIV Emergency Relief Project Grants	93.914
Workforce Investment Act ("WIA")	17.258, 17.259, 17.260
Head Start	93.600
Public Safety Partnerships and Community Policing Grants	16.710

8. A threshold of \$3,000,000 was used to distinguish between Type A and Type B programs as those terms are defined in OMB Circular A-133.
9. The Municipality did not qualify as a low-risk auditee as that term is defined in OMB Circular A-133.

PART II – SCHEDULE OF FINDINGS AND QUESTIONED COSTS:

Reference Number	Findings	Questioned Costs for the Year Ended June 30, 2005
Accounting and Finance Department		
05-01	Deficit in the Municipality's general fund at June 30, 2005.	\$ -
05-02	The Municipality is not taking the necessary steps to amortize or reduce the accumulated deficit in the general fund.	-
05-03	The Municipality is not canceling outstanding checks which have been outstanding for a period in excess of one year.	-
05-04	Inactive and unnecessary funds and accounts are not closed.	-
05-05	The Municipality's payroll register cannot be reconciled with its corresponding general ledger payroll and related benefit accounts.	-
05-06	Internal controls over property management needs to be strengthened.	-
All Federal Programs		
05-07	The Municipality does not prepare periodic certifications.	-
05-08	The Municipality does not have procedures in place to verify the status of an entity as to suspension and debarment when contracting services or procuring goods with federal funds.	-
05-09	The Municipality lacks adequate internal controls to ensure compliance with the earmarking, period of availability, and financial reporting compliance requirements.	-
Section 8 Housing Choice Vouchers		
05-10	The Municipality has not collected its accounts receivable from participants.	-
05-11	The Municipality lacks internal control over its Section 8 Housing Choice Voucher Program.	-
05-12	Policies and procedures for determination of participant's eligibility needs to be strengthened.	29,628
05-13	The Municipality did not comply with federal requirements regarding the determination and approval of participant's unit and its related rent.	-
05-14	The Municipality did not comply with federal requirements regarding the determination of housing assistance payments and lease approval.	12,176
05-15	The Municipality did not comply with federal requirements regarding the utility allowance schedule.	-
05-16	The Municipality did not comply with federal requirements regarding the selections from the waiting list.	-
05-17	The Municipality did not comply with federal requirements regarding housing quality standards inspections and enforcements.	2,221
05-18	Financial report submitted to HUD did not agree with the accounting records.	-
Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation		
05-19	The Municipality lacks of internal control over its Lower Income Moderate Rehabilitation Program.	-
05-20	Policies and procedures over the determination of eligibility need to be strengthened.	13,092
05-21	The Municipality did not comply with federal requirements regarding the utility allowance schedule.	-
05-22	Financial report submitted to HUD did not agree with the accounting records.	-
05-23	The Municipality did not submit the HUD 40118, Annual Progress Report.	-
05-24	The Municipality does not have adequate internal controls to ensure the current occupancy status of the units receiving program assistance.	-
Housing Opportunities for Persons with AIDS		
05-25	Controls over financial information included in reports submitted to the HUD need to be strengthened.	-
05-26	The Municipality does not have adequate internal controls over the evaluation of subgrantee proposals and monitoring of subrecipient's activities.	-
HOME Investment Partnership Program		
05-27	Financial records of the Municipality do not provide adequate information to separately identify program income earned by the HOME program.	-
05-28	Policies and procedures over determination of participant's eligibility needs to be strengthened.	-
	Sub-total	\$ 57,117 (continued)

Reference Number	Findings	Questioned Costs for the Year Ended June 30, 2005
	Balance forward	\$ 57,117
HOME Investment Partnership Program (cont.)		
05-29	The Municipality is not maintaining adequate controls over property and equipment items acquired by the HOME program.	-
05-30	The Municipality awarded a contractor for housing project not affordable to participants.	-
05-31	The Municipality of San Juan lacks of internal controls over tenant-based rental projects assisted with HOME funds.	-
HIV Emergency Relief Project Grants		
05-32	The Municipality is not maintaining adequate controls over property and equipment items acquired with federal funds.	-
Workforce Investment Act		
05-33	The cumulative financial reports submitted to the PRHRODC do not agree with the accounting records.	-
05-34	The Municipality is not maintaining adequate controls over property and equipment items acquired with federal funds.	-
Head Start		
05-35	The Municipality is not maintaining adequate controls over property and equipment items acquired by the Head Start Program.	-
	Total	<u>\$ 57,117</u>

MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART V

**FINDINGS ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON THE AUDIT
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

INTRODUCTION TO FINDINGS AND RECOMMENDATIONS

Background:

The findings and recommendations as defined in Parts V and VI and summarized in the schedule below, have been reviewed with representatives of the Municipality. The Municipality's corrective action plans will be submitted as part of the reporting package by the Municipality.

The following findings and recommendations often refer to the provisions of various authoritative documents, laws and regulations that were effective for the year ended June 30, 2005. The reference is to the documents at that date and does not reflect any changes resulting from subsequent amendments of the documents, laws and regulations. To avoid repeating their titles, following is the list of the documents with their respective titles and purposes, quoted in the findings and recommendations:

1. "OMB Circular A-87" - Circular A-87, issued by the Executive Office of the President, Office of Management and Budget, titled "Cost Principles for State and Local Governments," dated May 4, 1995 and further amended on August 29, 1997. This Circular Letter establishes the principles for determining the allowable costs of programs administered by state, local, and federally recognized Indian Tribal governments under grants from and contracts with the federal government.
2. "OMB Circular A-102" - Circular A-102, (Revised), issued by the Executive Office of the President, Office of Management and Budget, titled "Grants and Cooperative Agreements with State and Local Governments," dated October 7, 1994 and further amended on August 29, 1997. This Circular Letter establishes consistency and uniformity among federal agencies in the management of grants and cooperative agreements with state, local, and federally recognized Indian Tribal governments.
3. "OMB Circular A-133" - Circular A-133 as revised on June 30, 1997. This Circular Letter establishes uniform audit requirements for non-federal entities that administer federal awards and implements the Single Audit Act Amendments of 1996.
4. "The Act" - The Single Audit Act Amendments of 1996, Public Law 104-156, enacted on July 5, 1996, by the U.S. Congress. The Act was established to: a) promote sound financial management, including effective internal controls over federal awards; b) establish uniform requirements for audits of these programs; c) promote the efficient and effective use of audit resources; d) reduce burdens on auditees and e) ensure that the federal agencies and department's rely upon these audits.
5. "CFR" - This is the "Code of Federal Regulations" issued by the federal government. The CFR is a codification of the general and permanent rules published by the federal government. The code is divided into titles that represent broad areas subject to federal regulation. Each title is divided into chapters, which usually bear the name of the issuing agency, and is further subdivided into parts covering specific regulatory areas.
6. "Common Rule" - The Common Rule refers to the "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments" which establishes uniform administrative rules for Federal grants and cooperative agreements and subawards to State, local, and Indian Tribal governments.

7. "Basic Standards" - "The Revised Regulation on Basic Standards for the Municipalities of Puerto Rico" approved by the Office of the Commissioner of Municipal Affairs. The Basic Standards were created under Article 19.011 of Law 81, enacted on August 30, 1991, "Autonomous Municipalities Law". It establishes the rules and operational standards applicable to the municipalities in relation to the accountability of funds, property and other financial and fiscal matters administered by the municipalities of Puerto Rico. Its main purpose is to allow for the efficient use and administration of the municipal operations.
8. "Municipalities Law" - The "Autonomous Municipalities Law", Law 81 of August 30, 1991, as amended, was enacted to establish standard rules and regulations regarding the creation, organization, administration, and functions of the municipal governments in Puerto Rico. It establishes the main guidelines and requirements that govern all municipal functions and activities.

Corrective Action Plans:

The corrective action plans and responses to the findings and recommendations have been provided by the Municipality's representatives and reflect plans and responses as of March 31, 2006. These responses and corrective action plans were delivered to us after completion of our field work and, accordingly, our procedures with respect to such corrective action plans consisted of reading the Municipality's response. Although a few of the responses may indicate that the supporting documentation is available for examination, the finding is not eliminated because such evidence was found after we concluded the field work and, accordingly, we did not examine the aforementioned supporting information.

Questioned Costs:

The audit of compliance with laws and regulations, and the audit of the basic financial statements of the Municipality resulted in the identification of questioned costs totaling \$57,117 for the year ended June 30, 2005. For those instances where costs were questioned, the specific cost has been identified in the findings reported in the following pages.

The Schedule of Findings and Questioned Costs presented in Part IV, as listed in the table of contents, includes items arising from the Single Audit for the year ended June 30, 2005. Items that arose during the previous Single Audit that have yet to be resolved are included in Part VIII of this document. Questioned costs noted in the reports of federal auditors and proposed, or pending sanctions arising from programmatic reviews by federal agencies, if any, were reviewed to determine the nature of the item and its current status. This information was considered during the development of the current year's audit procedures. The final resolution of the items arising from other audits and reviews, as well as disposition of the questioned costs included in Part II, "Schedule of Findings and Questioned Costs," as listed in the table of contents, rests with the federal grantor agencies.

Reportable Conditions and Material Weaknesses:

The findings included in this report have been reported in accordance with the requirements of generally accepted government auditing standards (GAGAS), issued by the Comptroller General of the United States and Statements on Auditing Standards No. 60 and No. 74, issued by the Auditing Standards Board of the American Institute of Certified Public Accountants. These standards require the communication of all reportable conditions regarding an entity's internal control.

Reportable conditions are those matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operations of the internal control over compliance, which could adversely affect the Municipality's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grant agreements.

Finding Number 05-01

Department

Accounting and Finance Department

Category

Internal Control

Condition

The Municipality closed its fiscal year ended June 30, 2005 with a fund balance deficiency in the general fund of approximately \$35.2 million.

Criteria

Article 8.004 (b) of the Autonomous Municipalities Law establishes that the Municipality cannot obligate or spend funds in excess of the appropriations for the ensuing fiscal year. In addition, according to Chapter IV, Section 17, of the Basic Standards, the responsibility of oversight to prevent deficits in any municipal fund rests with the Finance Director.

Effects

The continued occurrence of this situation may result in possible significant fund limitations and eventual reduction or elimination of municipal services since future revenues will need to be used to pay for accumulated liabilities.

Cause

The above situation is primarily due to the fact that the Municipality is appropriating expenditures assuming revenues using the estimated tax collection projection provided by the Municipal Revenue Collection Center (the "Center"). Therefore, the Municipality enters into purchases and contracts for a total that exceeds the actual revenues earned and collected in property taxes. The budgeting system does not reflect actual revenues and therefore cannot prevent the obligation of expenditures for which current resources will not be available.

Recommendation

The Municipality should revise and amend the budget as current information related to collections of budgeted revenues became available in order to prevent incurring obligations in excess of available resources.

Views of Responsible Officials

Management agrees.

Finding Number 05-02

Department

Accounting and Finance Department

Category

Internal Control

Condition

The Municipality is not taking the necessary steps to amortize or reduce the accumulated deficit in the general fund, as required by law. The approved operational budget of the general fund for fiscal year 2004-05 included only \$500,000 to amortize the accumulated deficit.

Criteria

Article 7.011 of the Municipalities Law, as amended, requires that the municipalities with an accumulated deficit shall amortize such accumulated deficit during a period of no more than forty (40) years and, in case of an operational deficit for a given year after June 30, 1994, the Municipality should appropriate in its next year budget, an amount equal to the operational deficit for the immediately preceding year.

Effects

This situation will affect the Municipality's future ability to finance current operations since a significant amount of its future resources will already be committed to pay for expenditures incurred in previous years.

Cause

Including the required appropriation to amortize the accumulated deficit will result in a significant limitation of funds to pay current expenditures and obligations.

Recommendation

The Municipality should appropriate the necessary amount for each fiscal year in which such appropriation was not made in its current budget.

Views of Responsible Officials

Management agrees.

Finding Number 05-03

Department

Accounting and Finance Department

Category

Internal Control

Condition

The Municipality is not canceling outstanding checks which have been outstanding for a period in excess of one year.

Criteria

Chapter IV, Section 11, of the Basic Standards establishes that checks outstanding for more than one year should be cancelled. However, municipal checks, depending on the bank account used and nature of payment, there may be cases in which the Municipality issue checks with an expiration date ranging from three months to one year.

Effects

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

Cause

This is caused by the lack of regular monthly review of bank reconciliations and adequate follow up on reconciling items.

Recommendation

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

Views of Responsible Officials

Management agrees.

Finding Number 05-04

Department

Accounting and Finance Department

Category

Internal Control

Condition

Inactive and unnecessary funds and accounts are not closed. The Municipality is maintaining an excessive number of funds and accounts that have been inactive for a long period. The accounting records include various funds and accounts, many of which have been inactive or had insignificant operations during the year 2004-2005.

Criteria

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

Effects

The continued maintenance of these funds and accounts exposes the Municipality to the unauthorized use of funds from inactive accounts for activities not intended to be financed with these funds.

Cause

This situation occurs because the Municipality has not analyzed and closed inactive funds as well as the related bank accounts when the fund's objective have been achieved or are no longer of relevance.

Recommendation

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

Views of Responsible Officials

Management agrees.

Finding Number 05-05

Department

Accounting and Finance Department

Category

Internal Control

Condition

The Municipality's payroll register cannot be reconciled with the applicable expenditures recorded in the federal program funds...

Criteria

Article 8.010 (c) of the Municipality's Law states that the accounting system should provide: (a) complete results of the Municipality's operations; (b) proper and necessary financial information for the efficient administration of the Municipality; (c) effective controls and the accountability for all the funds, property and other municipal assets; and (d) necessary information for the preparation of accurate financial reports that could be used in the preparation of the municipal budget.

Effects

The above situation may result in the Municipality not detecting unauthorized payroll payments or payments to employees who are not working or performing duties directly related to the federal programs from which they are being paid. This may expose the Municipality to cost disallowances and actions from the awarding agencies.

Cause

The above situation was the result of payroll register having different account distributions than the general ledger.

Recommendation

Being payroll the most significant expenditure of the Municipality, necessary steps to correct this situation should be promptly taken. Consideration should be given to have payroll registers by program generated and reconciled, on a monthly basis, to the corresponding function and general ledger.

Views of Responsible Officials

Management agrees.

Finding Number 05-06

Department

Property Management

Category

Internal Control

Condition

Internal controls over property management needs to be strengthened. The Municipality is not performing annual inventories of its property and equipment. In addition, property records kept by the Municipality does not allow for them to be reconciled with the general ledger. According to the existing records of the Municipality, the cost of the property owned by the Municipality is approximately \$601.6 million as of June 30, 2005.

Criteria

Article 8.010 (c) of the Municipality's Law states that the accounting system should provide: (a) complete information of the Municipality's operations; (b) proper and necessary financial information for the efficient administration of the Municipality; (c) effective controls and the accountability for all the funds, property and other municipal assets; and (d) necessary information for the preparation of accurate financial reports that could be used in the preparation of the municipal budget.

Chapter VII, Section 22 of the Basic Standards also establishes that property physical inventories should be performed on an annual basis, as part of the overall property management control of the Municipality. Updated inventory lists should be compared and agreed with general ledger, and differences, if any, should be investigated and reconciled.

Effects

There is a significant risk of unauthorized use or disposition because there are no controls to ensure accountability of assets by department/division. This inadequate property control may expose the Municipality to cost disallowances by the federal government for lost or stolen federal property acquired with federal funds.

Cause

The Property Division has not enforced the requirement for the departments to both perform a property inventory and to ensure the proper accountability of assets.

Recommendation

A physical inventory of the Municipality's property should be performed as soon as possible for all departments and all differences should be investigated, adjusted and reconciled with the property recorded on the subsidiary ledgers. Federal regulations regarding disposition of property acquired with federal funds should be followed for property items which are not located as a result of such inventory.

Views of Responsible Officials

Management agrees.

MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART VI

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

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

ALL FEDERAL PROGRAMS

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the major programs tested. These general findings are relevant to all federal programs mentioned herein.

Finding Number 05-07

Category

Compliance/Internal Control

Compliance requirement

Allowable costs

Condition

The Municipality does not prepare periodic employee certifications for employees paid with federal funds to ensure that these employees are working and performing duties directly related to the Federal programs from which they are being paid.

Criteria

OMB Circular A-87, Attachment B, section 8(h)(3) establishes that charges for salaries and wages of employees that work solely on a single federal award or cost objective, must be supported by periodic certifications stating that the employees worked solely on that particular federal program for the period covered by the certification. These certifications should be prepared at least semi-annually and should be signed by the employee or supervisory official having first knowledge of the work performed by the employee.

Effects

Lack of controls over the time charges of personnel that are working on Federal programs could result in payments to employees who are not working or performing duties directly related to the Federal programs from which they are being paid.

Cause

The Municipality's management has not implemented proper control activities to ensure that the required certifications are obtained from employees and included in the respective human resource records.

Questioned Costs

None.

Recommendation

The Municipality's management should revise its internal control procedures to include obtaining periodic employee certifications that employees worked solely on a particular federal program. For employees that work on several financial assistance programs, certifications as to what programs they work for, should be obtained and their salaries allocated accordingly. Concurrently, a formal policy should be established by the Human Resources Department to track any changes in the tasks performed by employees and process the necessary adjustments to the employee's payroll on a timely basis.

Views of Responsible Officials

Management agrees.

Finding Number 05-08

Category

Internal Control

Compliance requirement

Procurement, suspension and debarment

Condition

The Municipality has not established a system of internal control to reasonably ensure compliance with procurement, suspension and debarment compliance requirements. During our audit we noted that the Municipality does not have procedures in place to verify the status of an entity as to suspensions and debarment when contracting services or procuring goods with federal funds. In testing procurement, suspension and debarment, the Municipality was not able to provide evidence indicating that procedures to assure that the individuals and entities that receive contracts or sub-awards are not suspended or debarred from participation in federal programs are being performed.

Criteria

OMB Circular A-102 establishes that federal assistance must not be awarded to any party which is debarred or suspended or is otherwise excluded from or ineligible for participation in Federal assistance programs under Executive Order 12549, "Debarment and Suspension". Agencies shall establish procedures for the effective use of the List of Parties Excluded from Federal Procurement or Non-procurement programs to assure that they do not award assistance to listed parties in violation of the Executive Order. Agencies shall also establish procedures to provide for effective use and/or dissemination of the list to assure that their grantees and subgrantees (including contractors) at any tier do not make awards in violation of the non-procurement, debarment and suspension common rule.

Effects

The Municipality could have procured goods or services from organizations and individuals that are suspended or debarred, which could result in cost disallowances by the federal awarding agency.

Cause

Current policies and procedures for procurement of goods and services are not designed to take into account the regulations applicable when purchases of goods or services are made with federal funds. As a result, the Municipality's personnel do not follow a standard procedure to ensure that entities or persons contracted are not suspended or debarred from federal procurement programs.

Questioned Costs

None.

Recommendation

The Municipality should amend their procurement procedures and include a step to verify whether or not the individual or entity is on the list of parties excluded from federal participation in procurement and non-procurement programs. The Municipality should also require the entities or individuals to submit a certification stating that they are not suspended or debarred.

Views of Responsible Officials

Management agrees.

Finding Number 05-09

Category

Internal Control

Compliance requirements

Earmarking

Period of availability

Reporting

Condition

Internal controls over accounting records needs to be strengthened to ensure compliance with the earmarking, period of availability, and financial reporting compliance requirements. During the performance of the audit we noted that:

- For most programs the Municipality's accounting records are not segregated according to type of expenditures (i.e. administrative costs), which need to be separately identifiable to ensure that the program complied with the minimum and/or maximum amount or percentage of the program's funding that must/may be used for specified activities and, thus, determine compliance with earmarking requirements. In these cases, a separate set of records is kept by the program to monitor such expenditures, resulting in two separate set of records for the same program. No periodic reconciliations are made over these two set of records.
- No formal controls are in place to monitor the period of availability requirements applicable to the different federal programs handled by the Municipality and thus ensure that all obligations are liquidated within their required period of availability.
- Monthly and year-end closing procedures over the accounting records are often not performed timely. As a result, financial records are not updated when financial reports are due, which may result in the submission of inaccurate or incomplete information to the applicable federal awarding agencies.

Criteria

OMB Circular A-102 requires grantees to have financial management systems that maintain effective control and accountability for all grant and subgrant cash, real and personal property, and other assets. Grantees and subgrantees must adequately safeguard all such property and must assure that it is used solely for authorized purposes. An effective internal control system should have a control structure in place in order to provide reasonable assurance that all disbursements paid with Federal funds are made in compliance the earmarking and period of availability requirements, and that financial reports submitted to federal awarding agencies are accurate and complete.

Effects

Lack of controls over these compliance requirements do not reasonably prevent instances of noncompliance with them, or allows for timely detection and correction of exceptions. The Municipality could be exposed to actions from Federal grantors, including disallowance of costs.

Cause

These situations are mostly caused due to the delay of the Municipality in closing the accounting periods. Due to this, program personnel are obligated to prepare their financial reports from alternate systems and unable to reconcile them properly with the general ledger. Furthermore, since the accounting records are not closed at the end of the periods for which these reports are prepared, the accounting records for such periods continue to change as subsequent transactions continue to be posted retroactively. No formal procedures exist to monitor or identify differences on financial reports previously submitted once an accounting period is closed.

Also, no formal procedures are in place by the personnel in charge of the disbursement procedures to ensure that a disbursement is processed within the required period of availability of the applicable program. The delay in the processing of transactions also increases the probability of paying or liquidating disbursements after the required period of availability.

Questioned Costs

None.

Recommendation

Procedures relating to compliance requirements should be strengthened and formally documented. Management should ensure that policies remain updated through periodic reviews. Formal documented policies need to be in place to enable management to guide employees on how to carry out their responsibilities.

In addition, the following specific procedures are recommended to ensure compliance with these Federal regulations:

Period of Availability:

The Municipality is responsible for ensuring that costs charged to the Federal programs result from obligations incurred during the funding period and that all obligations are liquidated before the liquidation deadline. Therefore, policies and procedures should be implemented to ensure that, before an obligation is made or a disbursement is processed, a member of management verifies that the transaction is being made within its period of availability.

In addition, improvements to the Municipality's accounting function and procedures would significantly minimize instances of noncompliance of this nature because many late disbursements may result due to the late processing of transactions. Management should improve its review process of the year-end closing procedures and implement rigorous time requirements to process transactions to ensure that all pending transactions are processed within the funding period and its corresponding liquidation deadline. In addition, closing procedures should be improved to ensure that all disbursements are posted to the correct accounts following the period of availability regulations.

Timely requests for extensions of the due dates may also be advisable when there exists the possibility that the failure to do so may result in noncompliance with this requirement.

Earmarking:

The Municipality should ensure that accounts used for recording expenditures of federal programs are adequate for segregation of expenditures to ensure compliance with the program applicable earmarking requirements.

Reporting:

The Municipality is responsible for ensuring that all information presented in reports submitted to the federal agencies are accurate and valid. Therefore, policies and procedures should be implemented to ensure that, before the financial reports are prepared and submitted, the information presented agrees to the Municipality's accounting records. Monitoring procedures should be implemented to timely submit amended reports, if needed, once accounting records are updated.

Improvements in the Municipality's accounting function and procedures would significantly minimize instances of noncompliance of this nature because inaccurate information presented generally results from the untimely processing of transactions and month-end and year-end accounting closings.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

SECTION 8 HOUSING CHOICE VOUCHERS – CFDA# 14.871

The Housing Choice Voucher Program (“HCVP”) provides rental assistance to help very low-income families afford decent, safe, and sanitary rental housing. The HCVP is administered by local public housing agencies (“PHAs”) authorized under State law to operate housing programs within an area or jurisdiction. The PHA accepts the application for rental assistance, selects the applicant for admission, and issues the selected family a voucher confirming the family’s eligibility for assistance. The family must then find and lease a dwelling unit suitable to the family’s needs and desires in the private rental market. The PHA pays the owner a portion of the rent (a housing assistance payment (“HAP”)) on behalf of the family.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the Section 8 Housing Choice Vouchers federal financial assistance program.

Finding Number 05-10

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance/Internal Control

Compliance requirements

Allowable costs/cost principles

Condition

The Municipality has not collected its accounts receivable from participants. The program has paid rental subsidies to owners on behalf of the participants that are in excess of the amounts they are entitled to receive, principally as a result of inaccurate information submitted by the participants, which was used to compute the housing assistance payment, resulting in unallowable costs.

Although the Municipality is currently performing certain collection efforts, at June 30, 2005, a balance of \$972,125 remained outstanding from prior years.

Criteria

24 CFR 570.200 and OMB Circular A-87 establish the various allowable activities to be financed with federal funds.

24 CFR 792 also encourages public housing agencies ("PHAs") to investigate and pursue instances of tenant and owner fraud and abuse in the operation of the Section 8 housing assistance payments programs.

Effects

The continued failure to collect the amounts owed by the participants may expose the Municipality to the possibility of being assessed penalties and interest costs on such amounts.

Cause

The above situation is the result of a lack of follow-up procedures and/or collection efforts that should be strengthened by the Municipality.

Questioned Costs

None, as these funds were already questioned in our 2004 report.

Recommendation

The Municipality should continue with the process to collect the amounts owed. Such process should be in accordance with the program's laws and regulations.

Views of Responsible Officials

Management agrees.

Finding Number 05-11

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Internal Control

Compliance requirements

Participant's eligibility

Financial reporting

Specials tests and provisions - selections from waiting list

Specials tests and provisions - utility allowance schedules

Specials tests and provisions - housing quality standards inspections

Specials tests and provisions - housing assistance payments

Specials tests and provisions - housing quality standards enforcements

Condition

The Municipality of San Juan does not have adequate internal controls over the following compliance requirements: participant's eligibility, financial reporting, selections from the waiting list, utility allowance schedules, housing quality standards inspections and enforcements, and housing assistance payments.

In testing compliance and internal controls over compliance for Section 8 Housing Choice Voucher Program we identified material instances of noncompliance over the abovementioned compliance requirements. The design of the procedures followed by the Program did not provide for the Municipality's personnel to prevent or timely detect these exceptions. For instances of noncompliance noted, refer to the following findings: 05-12 to 05-18.

Criteria

The A-102 Common Rule and OMB Circular A-110 require non-Federal entities receiving Federal awards (i.e., auditee management) to establish and maintain internal controls designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements.

Effects

The continued occurrence of this situation may result in the Municipality to be exposed to cost disallowances.

Cause

Although the Municipality's Administrative Plan for the Section 8 program covers policies and procedures that should be followed for each of the requirements described above, these policies are not always being followed. Procedures are sometimes overlooked and no proper monitoring exists to identify instances in which the adequate policies and procedures are not being followed.

Questioned Costs

None.

Recommendation

The Municipality should verify the internal control policies and procedures they have and modify them in order to address weaknesses on their design. A continued education program and or adequate segregation of duties should be implemented to ensure that personnel in charge of this program has the adequate knowledge over the program regulations. Supervisory roles should also be strengthened to verify the effectiveness of the internal controls.

Views of Responsible Officials

Management agrees.

Finding Number 05-12

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance / Internal Control

Compliance requirements

Eligibility

Condition

Policies and procedures for determination of participant's eligibility need to be strengthened.

In testing compliance and internal control over compliance with the requirement of participant's eligibility, we selected 58 participants who received HAP during FY 2004-05 to ascertain whether participants receiving HAP were eligible to participate in the program.

For 3 of the 58 participants selected (5%), we were unable to determine compliance with the abovementioned requirements as the Municipality could not provide us with the participant's file. Total HAP made to these participants during FY 2004-05 amounted to \$17,820.

For the remaining 55 participants tested, we noted the following instances of noncompliance and internal control deficiencies:

- Two (2) of the 55 participants (4%) were not eligible to participate in the program. Based on their annual adjusted income, they were not extremely low income families, as defined by the program's regulations. Total HAP made to these participants during FY 2004-05 amounted to \$8,576.
- Eight (8) of the 55 participants' files (15%) did not include the family member's consent forms authorizing the Municipality to examine documents to corroborate their status and income. Total HAP made to these participants during FY 2004-05 amounted to \$22,052. Such amount excludes HAPs made to participants for which we were able to examine third-party verification of income.
- For 19 of the 55 participants (35%), eligibility could not be determined due to missing information on the participant's files. The following information was not included in the files: (a) evidence of US citizenship such as birth certificates or social security cards (5 cases); (b) documents such as certifications of no criminal record or from education institutions used in the determination of the participant's eligibility status (14 cases); (c) missing documentation to support annual income, such as welfare and unemployment certifications (4 cases); and (d) inadequate documentation to support annual income (32 cases). A case may have had more than one exception. Inadequate documentation was noted on self-employment or unemployed applicants, for which a sworn statement signed by the participant declaring either their self-employment income or that no income was received during the base period were the only documents to support the applicant's income. However, no external documentation (i.e. income tax returns, etc.) is requested in order to corroborate the participant assertion. Total HAP made to these participants during FY 2004-05 amounted to \$60,337, excluding questioned costs included elsewhere.

- For 32 of the 55 participants (58%), the Municipality did not follow the required verification procedures to support the participant's annual income. Inadequate verification was noted on self-employed or unemployed applicants, for which a sworn statement signed by the participant declaring either their self-employment income or that no income was received during the base period was the only document to support the applicant's income. However, no external documentation (i.e. income tax returns, etc.) was requested in order to corroborate the participant assertion.

Other exceptions noted follows:

- *Participant application procedures.* For 18 out of the 55 participants (33%), the application form included in the participants' files was not signed by the applicant.
- *Documentation and examination of participant's eligibility.* The Municipality does not have computer matching mechanisms (i.e. automated comparison of data bases containing records about individuals) to identify undisclosed income sources.
- *Annual reexamination procedures.* In one case (2%) the participant file did not include the participant's agreement for the annual reexamination.

Criteria

Participant records. 24 CFR 982.158 requires a PHA to maintain complete and accurate accounts and other records for the program in accordance with HUD requirements, in a manner that permits a speedy and effective audit.

Participant application procedures. 24 CFR 982.158 requires the PHA to maintain during the term of each assisted lease, and for at least three years thereafter, the application from the family.

Documentation and examination of participant's eligibility. Per 24 CFR 982.201, the PHA may only admit an eligible family to the program. To be eligible, the applicant must be a citizen or a noncitizen who has eligible immigration status, and must be income-eligible.

In order to assert citizenship status, 24 CFR 5.216 and 5.218 and 24 CFR 982.552 require each assistance applicant to submit a valid social security card issued by the Social Security Administration. The PHA must deny the eligibility of an assistance applicant or participant, if they do not meet the applicable social security disclosure, documentation and verification, and certification requirements described above.

To be income-eligible, the Municipality has established in its administrative plan that based on the applicant's family adjusted income, only "extremely low income" families, as defined in 24 CFR 5.603, are eligible to participate in the program. Per 24 CFR 982.516, in the determination of adjusted income for an applicant, the PHA must obtain and document in the tenant file, third party verification of the following factors, or must document in the tenant file why third party verification was not available: (a) reported family annual income; (b) the value of assets; (c) expenses related to deductions from annual income; and (d) other factors that affect the determination of adjusted income. The PHA must establish procedures that are appropriate and necessary to assure that income data provided by applicant or participant families is complete and accurate. The procedures established in the Municipality's administrative plan require the verification of information submitted by the applicant through four methods of verification in the following order: (a) third party written; (b) third party oral; (c) review of documents; and (d) certification/self-declaration. If third-party written or oral verification is not available, or the information has not been verified by the third party within two weeks, the PHA should notate the file accordingly and utilize documents provided by the family as the primary source if the documents provide complete information.

24 CFR 982.553 also covers situations in which the PHA must prohibit admission to the program to certain criminal offenders and alcohol abusers. The Municipality's policies and procedures in place to ascertain that no criminal offenders covered by this section are improperly admitted to the program include the requirement to applicants to submit a certificate of criminal record as part of their eligibility review.

24 CFR 982.516 requires as a condition of admission to or continued assistance under the program, that the PHA shall require the family head, and such other family members as the PHA designates, to execute a HUD-approved release and consent form authorizing any depository or private source of income, or any Federal, State or local agency, to furnish or release to the PHA or HUD such information as the PHA or HUD determines to be necessary. 24 CFR 5.232 provides that if the applicant or participant, or any member of the applicant's or participant's family, does not sign and submit the consent form as required, then: (a) the processing entity shall deny assistance to and admission of an applicant; or (2) assistance to, and the tenancy of, a participant may be terminated.

Annual reexamination procedures. 24 CFR 982.516 requires a PHA to conduct a reexamination of family income and composition at least annually. The Municipality's policies and procedures to comply with this requirement include that participants must sign, during the admission process, a form acknowledging of this requirement.

Effects

The continued occurrence of this situation may result in the Municipality admitting ineligible participants to receive program benefits and, therefore, be exposed to cost disallowances.

Cause

All of the above matters occurred because the Municipality's internal control over this compliance requirement is not effectively identifying and correcting these matters through the proper review of participant files for completeness of documents, signatures and information, as well as for their accuracy.

Questioned Costs

Known questioned costs amounted to \$29,628. Additional potential questioned costs of \$87,049 were noted for participants for which we could not determine eligibility.

Recommendation

A complete and thorough analysis over the Municipality's procedures for participant's determination of eligibility should be made. The Municipality should ensure that all applicable requirements are being considered as part of these procedures and should also consider the development of a checklist that includes all the related documents and procedures that must be obtained and completed to determine eligibility for each participant. The checklist should be completed during the initial processing and should be revised for changes during the annual review. Once completed, the participant files should then be reviewed for completeness by another official or supervisor prior to the final approval. These procedures should improve controls and documentation concerning the eligibility of participants and will reduce the possibility of cost disallowances.

Views of Responsible Officials

Management agrees.

Finding Number 05-13

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance / Internal Control

Compliance requirement

Special tests and provisions - reasonable rent

Condition

The Municipality did not comply with federal requirements regarding the determination and approval of participant's unit and its related rent.

In testing compliance and internal control over compliance with the requirement of reasonable rent, we selected 58 participants who received HAP during FY 2004-05 to ascertain that rent of participants receiving HAP was reasonable.

For 3 of the 58 participants selected (5%), we were unable to determine compliance with the abovementioned requirement as the Municipality could not provide us with the participant's file. Total HAP made to these participants during FY 2004-05 amounted to \$17,820. No costs are questioned for these cases as they were already questioned in the eligibility finding.

For the remaining 55 participants tested, we noted the following instances of noncompliance and internal control deficiencies:

- In one case (2%) the participant's file did not include evidence that the Municipality reviewed comparable rents before approving the rent.
- In 14 cases (25%), the files examined did not include either HUD Form 50056, *Housing Assistance Voucher*, or HUD Form 52517, *Request for Tenancy Approval*.
- In five cases (9%), the number of bedrooms of the unit leased by the participant was not in accordance with the family members in household.

Criteria

24 CFR 982.507 states that a PHA may not approve a lease until the PHA determines that the initial rent to owner is a reasonable rent. At all times during the assisted tenancy, the rent to owner may not exceed the reasonable rent as most recently determined or redetermined by the PHA. The PHA administrative plan must cover the PHA policies on the method of determining that rent to owner is a reasonable rent per 24 CFR 982.54. 24 CFR 982.158 requires the PHA to keep for at least three years the records to document the basis for PHA determination that rent to owner is a reasonable rent (initially and during the term of a HAP contract) and other HUD-required reports.

24 CFR 982.402 also requires the PHA to establish subsidy standards that determine the number of bedrooms needed for families of different sizes and compositions. For each family, the PHA must then determine the appropriate number of bedrooms based on the PHA subsidy standards. The subsidy standards must provide for the smallest number of bedrooms needed to house a family without overcrowding and must be applied consistently for all families of like size and composition. The appropriate number of bedrooms for a family, as determined by the PHA under the PHA subsidy standards, is used to determine the maximum rent subsidy for a family assisted under the Voucher program.

Effects

The continued occurrence of this situation may result in the Municipality making housing assistance payments for units ineligible under the program guidelines, and therefore be exposed to cost disallowances.

Cause

All of the above matters occurred because the Municipality's internal control over this compliance requirement is not effectively identifying and correcting these matters through the proper review of participant files for completeness of documents, as well as for their accuracy.

Questioned Costs

None.

Recommendation

The Municipality should perform a complete and thorough analysis over its procedures for issuance of vouchers to applicants and tenancy approval. Modifications should be made on deficiencies noted to avoid their recurrence.

Views of Responsible Officials

Management agrees.

Finding Number 05-14

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance / Internal Control

Compliance requirements

Special tests and provisions - housing assistance payments

Condition

The Municipality did not comply with federal requirements regarding the determination of housing assistance payments and lease approval.

In testing compliance and internal control over compliance with the requirements of participant's eligibility, reasonable rent, and housing assistance payments ("HAP"), we selected 58 participants who received HAP during fiscal year 2004-05 to ascertain that participants receiving HAP were eligible to participate in the program and that HAP payments were reasonable and computed correctly.

For 3 of the 58 participants selected (5%), we were unable to determine compliance with the abovementioned requirements as the Municipality could not provide us with the participant's file. Total HAP made to these participants during FY 2004-05 amounted to \$17,820. No costs are questioned for these cases as they were already questioned in the eligibility finding.

For the remaining 55 participants tested, we noted the following instances of noncompliance and internal control deficiencies:

- For 16 of the 55 participants (29%), the HAP was calculated incorrectly, resulting in overpayments of \$13,338 during FY 2004-05 (\$8,744 if HAPs already questioned are excluded). Reasons for the errors in HAP calculation included: (a) annual adjusted income used for HAP computation was computed incorrectly (10 cases); (b) gross rent of units leased was higher than fair market rent (3 cases); and (c) lower of gross rent or payment standard was not used in HAP determination (3 cases).
- For six of the 55 participants (11%), the Municipality paid housing assistance payments although the related lease agreements were expired. The lease agreements of the Municipality are for a period of one year, however, they can be renewed automatically on a month to month basis, but no more than a period of three (3) years. Total HAP overpayments made after contract expiration amounted to \$19,678 (\$3,432 if HAPs already questioned are excluded).
- For four cases (7%), the rent per lease agreement did not agree with the rent per HUD Form 50058, *Housing Assistance Payment Computation*.
- For five cases (9%) the participant's file did not include either the lease agreement (4 cases) or a signed statement from the lessor and the participant acknowledging its responsibilities (1 case).
- Four lease agreements (7%) did not include either the Lease Addendum or the Lease Tenancy Addendum forms.

Criteria

24 CFR 982.505 addresses the calculation of housing assistance payment. A payment standard is used to calculate the monthly housing assistance payment for a family. The "payment standard" is the maximum monthly subsidy payment. The PHA shall pay a monthly housing assistance payment on behalf of the family that is equal to the lower of: (a) The payment standard for the family minus the total tenant payment; or (b) the gross rent (sum of the contract rent plus any utility allowance for the unit size leased) minus the total tenant payment. The payment standard for the family is the lower of: (a) the payment standard amount for the family unit size; or (b) the payment standard amount for the size of the dwelling unit rented by the family.

Per 24 CFR 982.503 the PHA must adopt a payment standard schedule that establishes voucher payment standard amounts for each fair market rent ("FMR") area in the PHA jurisdiction. For each FMR area, the PHA must establish payment standard amounts for each "unit size." Unit size is measured by number of bedrooms (zero-bedroom, one-bedroom, and so on).

Total tenant payment is defined by 24 CFR 5.628 as the highest of the following amounts, rounded to the nearest dollar: (a) 30 percent of the family's monthly adjusted income; (b) 10 percent of the family's monthly income; (c) if the family is receiving payments for welfare assistance from a public agency and a part of those payments, adjusted in accordance with the family's actual housing costs, is specifically designated by such agency to meet the family's housing costs, the portion of those payments which is so designated; or (d) the minimum rent, as determined in accordance with 24 CFR 5.630.

24 CFR 982.308(b) establishes that the term of the HAP contract begins on the first day of the lease term and ends on the last day of the lease term. 24 CFR 982.311 establishes that the housing assistance payments terminate if the lease terminate.

24 CFR 982.158 also requires the PHA to maintain during the term of each assisted lease, and for at least three years thereafter, a copy of the executed lease. These records should be complete and accurate.

Effects

The continued occurrence of this situation may result in the Municipality making housing assistance overpayments, and therefore be exposed to cost disallowances.

Cause

All of the above matters occurred because the Municipality's internal control over these compliance requirements are not effectively identifying and correcting these matters through the proper review of participant files for completeness of documents, signatures and information, as well as for their accuracy. The Municipality is also not verifying and amending unit lease contracts during the annual reexamination process of participants.

Questioned Costs

Known questioned costs amounted to \$12,176.

Recommendation

A complete and thorough analysis over the Municipality's procedures for determination of HAP calculations should be made. HAP calculations should be reviewed by a supervisor to determine that it was properly calculated and that factors used in their calculation, such as applicant's income and unit size, are both accurate and complete.

The Municipality should also verify all participants with expired housing unit lease agreements, and amend the contracts in order to cover the period until the next reexamination. Additionally, the Municipality should implement internal controls to verify that housing units lease agreements are valid until the next reexamination date.

Views of Responsible Officials

Management agrees.

Finding Number 05-15

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance

Compliance requirements

Special tests and provisions – Utility allowance schedule

Condition

The Municipality did not comply with federal requirements regarding the utility allowance schedule.

An analysis over utility allowances has not been made since 2001. Eventhough the schedule effective for FY 2004-05 was issued in October 2003, the rates included in said schedule were not determined in accordance with federal regulations as no evidence exists to support them.

Furthermore, the rates included in the latest utility schedule show a decrease when compared with the 2001 schedule, while the market conditions in Puerto Rico show an increasing trend in the cost of utilities.

We also noted during our tests over the participant's eligibility requirements that the utility allowances balances used by the Municipality are not consistent with the utility allowance schedules in effect.

Criteria

24 CFR 982.517 establishes that the Municipality must maintain an utility allowance schedule for all tenant-paid utilities (except telephone), for cost of tenant-supplied refrigerators and ranges, and for other tenant-paid housing services. The utility allowance schedule must be determined based on the typical cost of utilities and services paid by energy conservative households that occupy housing of similar size and type in the same locality. In developing the schedule, the Municipality must use normal patterns of consumption for the community as a whole and current utility rates.

This schedule must be reviewed each year, and the Municipality must revise its allowance for an utility category if there has been a change of 10 percent or more in the utility rate since the last time the schedule was revised. The Municipality must maintain information supporting its annual review of utility allowances and any revisions made in its utility allowance schedule.

Effects

The use of outdated utility allowance schedules may result in the granting of housing assistance payments to program participants for an incorrect amount.

Cause

The Municipality does not have adequate controls to ensure compliance with federal regulations regarding the utility allowance schedule due to lack of understanding over the applicable regulations.

Questioned Costs

None.

Recommendation

The Municipality should review and update its utility allowance schedule using the most recent information available. Prospectively, annual revisions to the allowance should be performed and documented in accordance with federal regulations.

Views of Responsible Officials

Management agrees.

Finding Number 05-16

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance

Compliance requirements

Special tests and provisions – selections from waiting list

Condition

The Municipality did not comply with federal requirements regarding the selections from the waiting list.

In testing compliance and internal control over compliance with the requirement for selecting participants from the waiting list, we selected 40 participants that were admitted to the Section 8 program during fiscal year 2004-05. We noted that for 100% of our sample, the Municipality did not follow the applicant selection policies established in its administrative plan as follows:

- Nine (9) out of the 40 participants selected (22.5%) were admitted to the program without being included in the waiting list first.
- 31 out of the 40 participants selected (77.5%) were admitted to the program even though they were not at the top of the waiting list. Other participants with the same or highest preference, and which applied earlier, were not considered first.
- We also selected an additional nine applicants at the top of the waiting list, noting that none of them (100%) were either admitted or provided with the opportunity to be admitted to the program although being located at the top of the list.

In addition, as part of our procedures for testing compliance and internal control over compliance with the participant's eligibility requirement, we selected 55 participants and noted that 23 of the 55 participants selected for testing were admitted to the program without being first included in the waiting list.

For none of these exceptions the Municipality documented the rationale used to admit the participants.

Other conditions noted during our examination of the waiting list follows:

- Applicants without social security number.
- Applicants in waiting list for which participant was changed in the system after application was processed.
- Numerical sequence on waiting list is interrupted without apparent explanation.
- Access to the participant's list master file was not restricted. A general password was known among personnel on the program and personnel which should not have access to modify the master file were given access to it.
- Participants included twice in the waiting list.
- Numerical sequence not followed based on application date.
- Unusual information on last update time.

Criteria

24 CFR 982.204 establishes that, except for special admissions targeted by HUD, participants to the Section 8 program must be selected from the Municipality's waiting list in accordance with the admission policies contained in the Municipality's administrative plan (the "Plan"). As per Section XII of the Municipality's administrative plan, at the time a housing voucher is available, the Municipality will select the family at the top of either the preference waiting list or the regular waiting list for admission to the program. Waiting list preferences are documented also in Section XII of the Plan.

Effects

The lack of adequate controls may result in the Municipality's denying other eligible applicants the opportunity of participating in the Section 8 program. Also, the continued failure over this compliance requirement may result in cost disallowances by the federal grantor or in the reduction of future grant awards because the overall program objectives may not be consistently met.

Cause

The Municipality does not have adequate controls to ensure compliance with federal regulations and the administrative plan when admitting participants to the Section 8 program.

Questioned Costs

None.

Recommendation

Internal controls and procedures over the selection of applicants from the waiting list should be revised to ensure that its design is effective in ascertaining compliance with federal regulations and those instances of noncompliance, if any, are detected on a timely basis to allow the Municipality to correct them promptly.

Views of Responsible Officials

Management agrees.

Finding Number 05-17

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance

Compliance requirements

Special tests and provisions – housing quality standards inspections

Special tests and provisions – housing quality standards enforcement

Condition

Housing quality standards ("HQS") inspections:

In testing compliance and internal control over compliance with the HQS inspections, we selected 15 units for which an annual reinspection was due during the fiscal year 2004-05. During our test we noted instances of noncompliance in 12 of our selections (80%), as follows:

- for two (2) out of the 15 units selected for testing (13%), no inspections were made during the fiscal year 2004-05. Total HAP made to these participants amounted to \$6,300, excluding HAPs already questioned.
- for seven (7) out of the 15 units selected for testing (47%), annual reinspections were done after the required timeframe.
- for three (3) out of the 15 units selected for testing (20%), the reinspections were done after the unit was reexamined.

In addition, as part of our procedures for testing compliance and internal control over compliance with the participant's eligibility requirement, we selected 55 participants and noted that: (a) for 20 cases (36%) the unit was approved and leased without being inspected first; (b) for five cases (9%), the inspection used for the unit approval was outdated, having more than 60 days at the time the unit was approved; and (c) for five cases (9%) the Municipality did not comply with HQS as they were either not inspected or the inspection was failed. No costs are questioned for these cases as they were already questioned in the eligibility finding.

HQS quality control:

In testing compliance and internal control over compliance with the HQS quality control requirements, we noted the following:

- Quality control procedures are not being done as documented in the PHA's Administrative Plan, which requires 15% of the inspections to be subject to quality control. Only 1% of the units were inspected under quality control procedures.
- Of the total 47 quality control inspections made during the fiscal year 2004-05, for 15 of them (32%) the quality control inspection reflected that the unit was not in compliance with HQS whereas the original inspection was passed by the Municipality inspector.
- For 11 out of the 47 quality control inspections made during fiscal year 2004-05, we were not able to conclude if the quality control was performed either because the quality control inspection was not documented on the participant's file or the participant's file was missing.

HQS enforcement:

In testing compliance and internal control over compliance with the enforcement of HQS, we selected 25 inspections made during the fiscal year 2004-05 which failed to comply with HQS in order to determine whether the Municipality enforced compliance with HQS within the required timeframe. For four (4) of the 25 inspections selected for testing (16%), we were unable to determine compliance with the abovementioned requirements as the Municipality could not provide us with the participant's file. Total HAPs made to these participants during FY 2004-05 amounted to \$20,208.

For the remaining 21 inspections examined, we noted the following instances of noncompliance:

- For ten of these 21 inspections (48%), the Municipality did not perform a subsequent inspection to verify if the owner corrected the deficiencies previously notified. Total HAPs made during FY 2004-05 for units that failed to meet HQS, after failed inspection date, amounted to \$24,053, excluding HAPs already questioned.
- For nine (9) of these 21 inspections (43%), the subsequent inspection to verify if the owner corrected the deficiencies previously notified was done after the required timeframe. In four of these nine inspections the PHA identified that the owner failed to correct the deficiencies, however, in none of these cases (100%) the Municipality did take any actions against these owners. Total HAPs made during FY 2004-05 for units that failed to meet HQS, after failed inspection date, amounted to \$2,221.

Criteria

24 CFR 982.404 to 405 requires a PHA to inspect a unit leased to a family at least annually during assisted occupancy to determine if the unit meets the HQS. An owner of a unit leased under this program is required to maintain the unit in accordance with HQS, as defined by 24 CFR 982.4. If the owner fails to maintain the dwelling unit in accordance with HQS, the PHA must take prompt and vigorous actions to enforce the owner obligations.

The PHA must not make any housing assistance payments for a dwelling unit that fails to meet the HQS, unless the owner corrects the defect within the period specified by the PHA and the PHA verifies the correction. If a defect is life threatening, the owner must correct the defect within no more than 24 hours. For other defects, the owner must correct the defect within no more than 30 calendar days.

The PHA must also conduct supervisory quality control HQS inspections.

Effects

The Municipality might be incorrectly issuing housing assistance payments for sub-standard housing units which would otherwise be ineligible for participation under the Section 8 program.

Cause

The Municipality does not have adequate internal controls to ensure that HQS inspections, quality control, and enforcement procedures are in accordance with federal requirements. Major deficiencies noted included the following:

- Each time an inspection is made, the related information (including if it failed or passed, and the inspection date) is entered into the system and a report is prepared with the inspections due during a specified period. However, this report is not used by the Municipality to monitor that reinspections are done timely due to a lag in the processing of inspections in the system (i.e., system information is not updated).
- The number of employees working with the inspections appears to be inadequate considering the volume of units administered by the program. The Municipality has only three inspectors for approximately 4,000 units under the program.

Questioned Costs

Known questioned costs amounted to \$2,221. Additional potential questioned costs due to units in which were either not inspected or for which HQS deficiencies were noted and not corrected amounted of \$50,561.

Recommendation

The Municipality should perform a thorough analysis of the current HQS procedures and modify their design as deemed necessary to ensure that HQS inspections, quality control, and enforcement procedures are done as required by federal regulations.

Views of Responsible Officials

Management agrees.

Finding Number 05-18

Federal program

Section 8 Housing Choice Voucher Program, CFDA #14.871

Category

Compliance

Compliance requirements

Reporting – Financial reporting

Condition

The Municipality is required to submit to HUD on a quarterly basis the Form HUD-52861, *Voucher for Payment of Annual Contributions and Operating Statement*. During our procedures over the correctness of the information provided in said report, we noted that the financial data submitted did not agree with the financial records of the Municipality.

Criteria

HUD regulations require PHAs to submit form HUD-52681 to the HUD Financial Management Center. Among the information required to be presented on this form, the PHA must report the operating income, operating expenditures, and operating reserve of the PHA for the reporting period.

Effects

Failure to report accurate information prevents HUD from monitoring the performance of the program's financial activities, assessing the achievements of those programs and evaluating the expected grant award for the following years.

Cause

The Municipality does not have adequate internal controls in order to ensure that financial data used in reports submitted to federal awarding agencies is accurate.

Questioned Costs

None.

Recommendation

The Municipality should design procedures to ensure that reports submitted to federal awarding agencies are both complete and accurate.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

**LOWER INCOME HOUSING ASSISTANCE PROGRAM
SECTION 8 MODERATE REHABILITATION - CFDA # 14.856**

The objective of the Section 8 rental assistance programs is to help eligible low-income families or individuals obtain decent, safe, and sanitary housing through a system of rental subsidies. Under this project-based cluster, the rental subsidy is tied to a specific unit and when a family moves from the unit, it has no right to continued assistance.

The following findings and recommendations arise from our tests of compliance and internal control over compliance with requirements applicable to the Lower Income Housing Assistance Program.

Finding Number 05-19

Federal program

Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation, CFDA # 14.856

Category

Internal Control

Compliance requirements

Participant's eligibility

Financial reporting

Specials tests and provisions - utility allowance schedules

Specials tests and provisions - housing quality standards inspections

Specials tests and provisions - housing assistance payments

Specials tests and provisions - housing quality standards enforcements

Condition

The Municipality of San Juan does not have adequate internal controls over the following compliance requirements: participant's eligibility, financial reporting, utility allowance schedules, housing quality standards inspections and enforcements, and housing assistance payments. In testing compliance and internal control over compliance for the Lower Income Housing Assistance Program we identified material instances of noncompliance over the abovementioned compliance requirements. The design of the procedures followed by the Program did not provide for the Municipality's personnel to prevent or timely detect these exceptions. For instances of noncompliance noted, refer to the following findings: 05-20 to 05-24.

Criteria

The A-102 Common Rule and OMB Circular A-110 require non-Federal entities receiving Federal awards (i.e., auditee management) to establish and maintain internal controls designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements.

Effects

The continued occurrence of this situation may result in the Municipality to be exposed to cost disallowances.

Cause

Although the Municipality's Administrative Plan for the Lower Income Moderate Housing Assistance – Section 8 Moderate Rehabilitation program covers policies and procedures that should be followed for each of the requirements described above, these policies and procedures are not always followed. Procedures are sometimes overlooked and no proper monitoring exists to identify instances in which the existing policies and procedures are not being followed.

Questioned Costs

None.

Recommendation

The Municipality should verify the internal control policies and procedures they have and modify them in order to address weaknesses on their design. A continued education program and an adequate segregation of duties should be implemented to ensure that personnel in charge of this program has the adequate knowledge over the program regulations. Supervisory roles should also be strengthened to verify the effectiveness of the internal controls.

Views of Responsible Officials

Management agrees.

Finding Number 05-20

Federal program

Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation, CFDA # 14.856

Category

Compliance / Internal Control

Compliance requirements

Eligibility

Condition

Policies and procedures over the determination of eligibility need to be strengthened. In testing compliance and internal control over compliance with the requirement of participant's eligibility, reasonable rent, and housing assistance payments ("HAP"), we selected 25 participants who received HAP during fiscal year 2004-05 to ascertain whether participants receiving HAP were eligible to participate in the program and that HAP payments were reasonable and computed correctly.

For the 25 participants tested, we noted the following instances of noncompliance and internal control deficiencies:

- Three (3) of the 25 participants' files selected (12%) were not eligible to participate of the program since they did not include the family member's consent forms authorizing the Municipality to examine documents to corroborate their status and income. Total HAP made to these participants during FY 2004-05 amounted to \$9,662.
- For 10 of the 25 participants selected (84%), the HAP was calculated incorrectly, resulting in overpayments of \$3,430 during FY 2004-05 due to errors in the determination of the adjusted income used for HAP computation.
- For eight (8) of the 25 participants selected (32%), eligibility could not be determined due to missing information on participant's files. The following information was not included in the files: (a) evidence of US citizenship such as birth certificates or social security cards (3 cases); (b) documents such as certifications of no criminal record or participant sworn statements used in the determination of the participant's eligibility status (2 cases); and (c) missing documentation to support annual income, such as welfare certifications (2 cases); and (d) inadequate documentation to support annual income, such as welfare certifications or participants sworn statements (4 cases). A case may have had more than one exception. Total HAP made to these participants during FY 2004-05 amounted to \$28,454, excluding HAP already questioned.
- For 21 of the 55 participants selected (84%), the Municipality did not follow the required verification procedures to support the participant's annual income. Inadequate verification was noted on self-employed applicants, for which a sworn statement signed by the participant declaring either their self-employment income or that no income was received during the base period was the only document to support the applicant's income. However, no external documentation (i.e. income tax returns, etc) was requested in order to corroborate the participant assertion.

Other exceptions noted follows:

- *Participant application procedures.* For two (2) out of the 25 participants selected (8%), the application form was not included in the participant's file. In addition, ten out of the 25 participants (40%) were admitted to the program without being included in the waiting list first.
- *Documentation and examination of participant's eligibility.* The Municipality does not have computer matching mechanisms (i.e. automated comparison of data bases containing records about individuals) to identify undisclosed income sources.
- *Annual reexamination procedures.* In one case (4%) the participant file did not include the participant's agreement for the annual reexamination. In another case (4%) the annual reexamination was not performed when due.
- *HQS Procedures.* For three (3) of the 25 participants (12%), either the housing unit inspection performed during the initial admission or reexamination process shows a failed status (2 cases) or no evidence of inspection was noted on participant's file (one case); however the Municipality provided assistance to these participants.

Criteria

Participant application procedures. 24 CFR 882.513(b) requires the public housing agency ("PHA") to maintain a waiting list for applicants for the Moderate Rehabilitation Program. 24 CFR 882.514 states that when vacancies occur, the PHA should refer to the owner one or more appropriate size families from its waiting list. The PHA must select families for participation in accordance with the provisions of the Program and in accordance with the PHA's application.

Documentation and examination of participant's eligibility. 24 CFR 882.514 states that the PHA is responsible for the receipt and review of applications, and determination of family eligibility for participation in accordance with HUD regulations. To be eligible, the applicant must be a citizen or a noncitizen who has eligible immigration status, and must be income-eligible.

In order to assert citizenship status, 24 CFR 5.216 and 5.218 and 24 CFR 882.515 require each assistance applicant to submit a valid social security card issued by the SSA. The PHA must deny the eligibility of an assistance applicant or participant, if they do not meet the applicable social security disclosure, documentation and verification, and certification requirements described above.

To be income-eligible, the applicant's family should be considered low-income, as defined in 24 CFR 5.603. In order to determine the income eligibility, per 24 CFR 882.514 the PHA is responsible for verifying the sources and amount of the family's income and other information necessary for determining income eligibility and the amount of the assistance payment. 24 CFR 5.232 also provides that if the applicant or participant, or any member of the applicant's or participant's family, does not sign and submit a consent form authorizing any depository or private source of income, or any Federal, State or local agency, to furnish or release to the PHA or HUD such information as the PHA or HUD determines to be necessary, then: (a) the processing entity shall deny assistance to and admission of an applicant; or (2) assistance to, and the tenancy of, a participant may be terminated.

24 CFR 882.518 also covers situations in which the PHA must prohibit admission to the program to certain criminal offenders. The Municipality's policies and procedures in place to ascertain that no criminal offenders covered by this section are improperly admitted to the program include the requirement to applicants to submit a certificate of criminal record as part of their eligibility review.

Annual reexamination procedures. 24 CFR 882.515 requires a PHA to conduct a reexamination of family income and composition at least annually. The Municipality's policies and procedures to comply with this requirement include that participants must sign, during the admission process, a form acknowledging of this requirement.

Effects

The continued occurrence of this situation may result in the Municipality admitting ineligible participants to receive program benefits or making housing assistance overpayments and, therefore, be exposed to cost disallowances.

Cause

All of the above matters occurred because the Municipality's internal control over these compliance requirements are not effectively identifying and correcting these matters through the proper review of participant files for completeness of documents, signatures and information, as well as for their accuracy.

Questioned Costs

Known questioned costs amounted to \$13,092. Additional potential questioned costs of \$28,454 were noted for participants for which we could not determine eligibility.

Recommendation

A complete and thorough analysis over the Municipality's procedures for participant's determination of eligibility and HAP calculations should be made. The Municipality should ensure that all applicable requirements are being considered as part of these procedures and should also consider the development of a checklist that includes all the related documents and procedures that must be obtained and completed for each participant. The checklist should be completed during the initial processing and should be revised for changes during the annual review. Once completed, the participant files should then be reviewed for completeness by another official or supervisor prior to the final approval. These procedures should improve controls and documentation concerning the eligibility of participants and will reduce the possibility of cost disallowances.

Views of Responsible Officials

Management agrees.

Finding Number 05-21

Federal program

Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation, CFDA # 14.856

Category

Compliance

Compliance requirements

Special tests and provisions – Utility allowance schedule

Condition

The Municipality did not comply with federal requirements regarding the utility allowance schedule. In testing compliance and internal control compliance with the utility allowance schedule requirements, we noted that an analysis over utility allowances has not been made since 2001. Even though the schedule effective for FY 2004-05 was issued in October 2003, the rates included in said schedule were not determined in accordance with federal regulations as no evidence exists to support them. Furthermore, the rates included in the latest utility schedule show a decrease when compared with the 2001 schedule, while the market conditions in Puerto Rico show an increasing trend in the cost of utilities.

We also noted during our tests over the participant's eligibility requirements that the utility allowances balances used by the Municipality are not consistent with the utility allowance schedules in effect. Additionally, we noted that the Municipality paid amounts to participants that are not consistent with the amounts per schedule and did not apply correctly the utility allowance to participants.

We also selected 25 participants who received utility allowances during FY 2004-05 and noted the following exceptions:

- In four (4) of the 25 cases examined (16%), the participant file did not include a request from the participant to receive utility allowances.
- In 13 of the 25 cases examined (52%), the utility allowance paid to the participant was in excess of those established in the Municipality's schedule in effect. Total questioned costs (known or likely) due to these overpayments did not exceed \$10,000.

Criteria

24 CFR 882.510 requires a PHA to determine, at least annually, whether an adjustment is required in the utility allowance applicable to the dwelling units in the program, on grounds of changes in utility rates or other change of general applicability to all units in the program. The PHA may also establish a separate schedule of allowances for each building of 20 or more assisted units, based upon at least one year's actual utility consumption data following rehabilitation under the Program. If the PHA determines that an adjustment should be made in its schedule of allowances or if it establishes a separate schedule for a building which will change the allowance, the PHA must then determine the amounts of adjustments to be made in the amount of rent to be paid by affected families and the amount of housing assistance payments and must notify the owners and families accordingly. Any adjustment to the allowance must be implemented no later than the family's next reexamination date or lease renewal date, whichever is earlier.

Effects

The use of outdated utility allowance schedules may result in the granting of housing assistance payments to program participants for an incorrect amount.

Cause

The Municipality does not have adequate controls to ensure compliance with federal regulations regarding the utility allowance schedule due to lack of understanding over the applicable regulations.

Questioned Costs

None.

Recommendation

The Municipality should review and update its utility allowance schedule using the most recent information available. Prospectively, annual revisions to the allowance should be performed and documented in accordance with federal regulations. Provisions should be taken to ensure that utility allowances granted to participants are in accordance with utility schedules in effect at the time of the request.

Views of Responsible Officials

Management agrees.

Finding Number 05-22

Federal program

Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation, CFDA # 14.856

Category

Compliance

Compliance requirements

Reporting – Financial reporting

Condition

Procedures over reconciliation and verification of financial data submitted to the HUD needs to be strengthened.

The Municipality is required to submit to HUD on a annually basis the Form HUD-52861, *Voucher for Payment of Annual Contributions and Operating Statement*. During our procedures over the correctness of the information provided in said report, we noted that the financial data submitted did not agree with the financial records of the Municipality.

Criteria

HUD regulations require PHAs to submit form HUD-52681 to the HUD Financial Management Center. Among the information required to be presented on this form, the PHA must report the operating income, operating expenditures, and operating reserve of the PHA for the reporting period.

Effects

Failure to report accurate information prevents HUD from monitoring the performance of the program's financial activities, assessing the achievements of those programs and evaluating the expected grant award for the following years.

Cause

The Municipality does not have adequate internal controls in order to ensure that financial data used in reports submitted to federal awarding agencies is accurate.

Questioned Costs

None.

Recommendation

The Municipality should design procedures to ensure that reports submitted to federal awarding agencies are both complete and accurate.

Views of Responsible Officials

Management agrees.

Finding Number 05-23

Federal program

Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation, CFDA # 14.856

Category

Compliance

Compliance requirements

Reporting – Financial reporting

Condition

The Municipality did not submit during FY 2004-05 the Form HUD-40118, *Annual Progress Report* (“APR”) for the Moderate Rehabilitation Single Room Occupancy projects.

Criteria

HUD regulations require PHAs to submit form HUD-40118 to the HUD within 90 days after the end of each operating year.

Effects

Failure to submit an APR may delay receiving grant funds and may result in a determination of lack of capacity for future funding.

Cause

Due to lack of personnel, this report has not been prepared and submitted to the HUD. Limited resources available have been used primarily for the operations of other types of assistance received from the Moderate Rehabilitation program.

Questioned Costs

None.

Recommendation

Form HUD-40118 should be prepared immediately and submitted to the HUD.

Views of Responsible Officials

Management agrees.

Finding Number 05-24

Federal program

Lower Income Housing Assistance Program – Section 8 Moderate Rehabilitation, CFDA # 14.856

Category

Internal control

Compliance requirements

Special tests and provisions – Vacant units

Condition

The Municipality does not have adequate internal controls to ensure the current occupancy status of the units receiving program assistance. No policies and procedures are in place to detect units vacated and not notified to the Municipality.

Criteria

24 CFR 882.411 states that if an eligible family vacates its unit, the owner of the unit may receive HAP due under their contract for the month in which unit becomes vacant and 80% of the contract rent for an additional month, as long as the unit remains vacant. However, if the owner does not notify the PHA immediately of the vacancy, then the owner is not entitled to any payment.

Effects

Unallowable payments may be disbursed for units which are not being occupied by eligible families.

Cause

Due to lack of personnel, the Municipality has emphasized the use of their resources in other areas that they consider to be of more priority.

Questioned Costs

None.

Recommendation

The Municipality should verify the internal control policies and procedures they have and modify them in order to address weaknesses in their design. Responsibilities assigned to current personnel should be evaluated and more personnel should be assigned to this program in order to comply with federal requirements, as deemed necessary. Supervisory roles should be strengthened to verify the effectiveness of the internal controls.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

HOUSING OPORTUNITIES FOR PERSONS WITH AIDS - CFDA # 14.241

The Housing Opportunities for Persons with AIDS ("HOPWA") Program is designed to provide States and localities with resources and incentives to devise long term strategies for meeting the housing needs of persons with acquired immunodeficiency syndrome ("AIDS") or related diseases and their families (24 CFR section 574.3).

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

Finding Number 05-25

Federal program

Housing Opportunity for Persons with AIDS, CFDA # 14.241

Category

Internal Control

Compliance requirement

Reporting

Condition

Controls over financial information included in reports submitted to the HUD need to be strengthened. During our tests on compliance and internal control over compliance with the reporting requirement, we noted that the expenditures amount shown on the Financial Summary included within the Consolidated Annual Performance and Evaluation Report ("CAPER") is obtained from the HUD's system Integrated Disbursements and Information System ("IDIS"). However, said data is not reconciled to the Municipality's general ledger. As of June 30, 2005 differences were noted between these two systems.

Criteria

24 CFR 85.20(b)(1) establishes that accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or subgrant.

Effects

The continued occurrence of this situation prevents the awarding agency from monitoring the program's financial performance. In addition, the Municipality could be sanctioned by the federal awarding agency due to the inaccurate filing of federal financial reports.

Cause

The above situation resulted because program' management assessment was that the program is only required to inform expenditures as per the IDIS system and that reconciliations with general ledger were not necessary to support the accuracy of the information obtained from IDIS.

Questioned Costs

None.

Recommendation

The Municipality should perform timely reconciliation and cutoff procedures between numbers kept at the federal programs and numbers recorded in the Municipality's general ledger in order to obtain reasonable assurance that financial reports submitted to the federal awarding agency include all activities of the reporting period, are supported by underlying accounting or performance records, and are fairly presented in accordance with program requirements.

Views of Responsible Officials

Management agrees.

Finding Number 05-26

Federal program

Housing Opportunity for Persons with AIDS, CFDA # 14.241

Category

Compliance / Internal Control

Compliance requirements

Allowable costs

Subrecipient monitoring

Condition

The Municipality does not have adequate internal controls over the evaluation of subgrantee proposals and monitoring of subrecipient's activities. During our tests on compliance and internal controls over compliance with the subrecipient's monitoring requirement, we selected 16 subgrantees and noted the following deficiencies:

Awarding of funds

- Three subrecipients were approved assistance during the fiscal year 2004-05 although they had not complied with the submission of single audit reports for prior award years or single audit reports submitted reflected material weaknesses or reportable conditions.

Monitoring of funds

- For eight (8) of the 16 subrecipients examined (50%), we were not provided with evidence of the agreement between the Municipality and the subgrantee. No evidence was provided that the Municipality made these subrecipients aware of the award information and requirements pertaining to the program.
- For 15 of the 16 subrecipients examined (94%), no documentation could be provided with regards to the monitoring procedures performed by the Municipality.
- For 15 of the 16 subrecipients examined (94%), no adequate follow up was given to subrecipient single audit reports as follows: (a) the Municipality had not received single audits reports (2 cases); or (b) an updated single report has not been submitted by the subrecipient (13 cases). Total funds awarded to these subrecipients amounted to \$3,138,869. In addition, no formal evidence exists of the review performed over single audit reports received and that such review was made within six months of their receipt, as required by Federal regulations.
- Latest single audit reports on file for nine subrecipients reflected reportable conditions, material weaknesses and/or questioned costs. For seven of these subrecipients (78%), the Municipality has neither received a corrective action plan nor sanctioned them due to noncompliance with this requirement.

Criteria

The requirements for subrecipient monitoring are contained in the Single Audit Act Amendments of 1996, Section .225 and .400(d) of the OMB Circular A-133, and Section .37 and .40(a) of A-102 Common Rule. Per these regulations, a pass-through entity is responsible for:

- *Award Identification.* At the time of the award, identifying to the subrecipient the Federal award information (e.g., CFDA title and number, award name, name of Federal agency) and applicable compliance requirements.

- *During-the-Award Monitoring* - Monitoring the subrecipient's use of Federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers Federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- *Subrecipient Audits* - (1) Ensuring that subrecipients expending \$500,000 or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of OMB Circular A-133 and that the required audits are completed within 9 months of the end of the subrecipient's audit period, (2) issuing a management decision on audit findings within 6 months after receipt of the subrecipient's audit report, and (3) ensuring that the subrecipient takes timely and appropriate corrective action on all audit findings. In cases of continued inability or unwillingness of a subrecipient to have the required audits, the pass-through entity shall take appropriate action using sanctions.
- *Pass-Through Entity Impact* - Evaluating the impact of subrecipient activities on the pass-through entity's ability to comply with applicable Federal regulations.

In addition, the A-102 Common Rule and OMB Circular A-110 require that non-Federal entities receiving Federal awards (i.e., auditee management) to establish and maintain internal controls designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements. Adequate internal controls should provide reasonable assurance that subrecipient activities are monitored, subrecipient audit findings are resolved, and the impact of any subrecipient noncompliance on the pass-through entity is evaluated.

Effects

Inadequate monitoring procedures may expose the Municipality to the risk that unallowable use of funds are not detected and corrected on a timely basis. Noncompliance could result in the loss of Federal funds. Additionally, program objectives may not be achieved, as timely monitoring of subgrantee performance is not adequately performed.

Cause

Although the Municipality's has in place various tools to approve and monitor subgrantees, such as proposals evaluation guides and checklists, and single audit requests forms to subrecipients, their use is not consistent. Procedures are sometimes overlooked and no proper monitoring exists to identify instances in which the adequate policies and procedures are not being followed.

In addition, during FY 2004-05 personnel previously assigned to the monitoring of HOPWA subrecipients were relocated to other functions. No resources were allocated to HOPWA program to cover these vacancies.

Questioned Costs

None.

Recommendation

The Municipality should verify the internal control policies and procedures they have and modify them in order to address weaknesses on their design. Proper training to employees and established segregation of duties should be implemented to ensure that personnel in charge of this program have the adequate knowledge over the program regulations. Supervisory roles should be strengthened to verify the effectiveness of the internal controls. The following guidelines should be considered:

- Single audit reports should be obtained within the required time frame and its corresponding review should be performed and documented on a timely basis. The preparation of a review tool, such as a checklist is advisable. Management decisions resulting from this review should be clearly documented, as well as follow-up activities performed on single audit findings.

- Develop and implement policies to ensure that files are adequate and consistent and to ascertain that they include support for conclusions in monitoring reports. Subrecipient files should also include documentation on follow-up procedures performed on corrective action implementation.
- Develop a tracking system that alerts staff of approaching deadlines for reports and corrective action plans. Follow up aggressively to obtain acceptable corrective action plans in a timely manner. Subrecipient tracking documents should be developed and maintained for management decision and audit purposes.
- Review current monitoring guides to ensure that they include steps to obtain reasonable assurance that subrecipients are complying with applicable Federal regulations. In addition, the Municipality should assign sufficient resources to enable the performance of adequate monitoring of the subrecipients, specifically for the programmatic area.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

HOME INVESTMENT PARTNERSHIP PROGRAM - CFDA # 14.239

The objectives of the Home Investment Partnership Program ("HOME") include: expanding the supply of decent and affordable housing, particularly housing for low and very low-income Americans; strengthening the abilities of State and local governments to design and implement strategies for achieving adequate supplies of decent, affordable housing; providing financial and technical assistance to participating jurisdictions, including the development of model programs for affordable low-income housing; and extending and strengthening partnerships among all levels of government and the private sector, including for-profit and not for profit organizations, in the production and operation of affordable housing (24 CFR section 92.1).

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

Finding Number 05-27

Federal program

Home Investment Partnership Program, CFDA # 14.239

Category

Compliance

Compliance requirements

Program Income

Reporting

Condition

Financial records of the Municipality do not provide adequate information to separately identify program income earned by the HOME program. Currently, all types of program income generated are recorded in the accounting records as direct reductions to the expenditure accounts and no separate accounts are maintained to account for them.

Criteria

Per 24 CFR 92.508, each participating jurisdiction ("PJ") must establish and maintain sufficient records to enable HUD to determine whether the PJ has met the requirements of this part. At a minimum, the PJ must have financial records identifying the source and application of program income, repayments, and recapture funds. Although separate program income records are maintained by the public housing agency in charge of this program, these are not reconciled with the general ledger.

Effects

Failure to record accurate information prevents the Municipality from monitoring the performance of the program's financial activities, and assessing the achievements of the program.

Cause

A separate account for program income was not been created for this program.

Questioned Costs

None.

Recommendation

Separate general ledger accounts should be created to account for the income generated by the program.

Views of Responsible Officials

Management agrees.

Finding Number 05-28

Federal program

Home Investment Partnership Program, CFDA # 14.239

Category

Compliance

Compliance requirements

Eligibility

Earmarking

Condition

Policies and procedures over determination of participant's eligibility need to be strengthened. In testing compliance and internal control over compliance with the requirements of participant's eligibility, we selected 24 participants which received HOME homebuyer assistance during fiscal year 2004-05 to ascertain that participants receiving federal assistance were eligible to the program. We noted that in four (4) cases of the 24 applicants tested (17%), eligibility could not be determined due to missing information on participant's files. Information not included on files included: (a) evidence of US citizenship such as birth certificates or social security cards (2 cases); and (b) missing documentation to support annual income, such as latest income tax returns (3 cases). A case may have had more than one exception. Total HAP made to these participants during FY 2004-05 amounted to \$219,307.

Criteria

24 CFR 92.217 states that PJs must invest 100 percent of HOME funds made available during a fiscal year so that with respect to homeownership assistance in dwelling units that are occupied by households that qualify as low-income families.

Effects

The continued occurrence of this situation may result in the Municipality admitting ineligible participants to receive program benefits and, therefore, be exposed to cost disallowances.

Cause

No standard procedures are in place to ensure that all required documents and analysis are obtained prior to admitting a participant to the program.

Questioned Costs

Potential questioned cost of \$219,307 was noted for participants for which we could not determine eligibility.

Recommendation

Review over information required to determine income should be strengthened to ensure that the Municipality is obtaining all required documents to validate income before the application is approved. This procedure should improve controls and documentation concerning the eligibility of participants and will reduce the possibility of cost disallowances.

Views of Responsible Officials

Management agrees.

Finding Number 05-29

Federal program

Home Investment Partnership Program, CFDA # 14.239

Category

Compliance

Compliance requirements

Equipment and Real Property Management

Condition

The Municipality is not maintaining adequate controls over property and equipment items acquired by the HOME program. In testing compliance and internal controls over compliance with the equipment and real property management requirement, the following deficiencies were noted:

- The property and equipment records provided did not contain the condition of the property.
- Property records could not be reconciled with general ledger amounts.
- There are no established procedures or controls that ensure an immediate update of property records when an item of property or equipment is either transferred from one location to another or is disposed of. Without this information the Municipality does not know if it is responsible for compensating the corresponding Federal awarding agencies for their share of any property sold or converted to non-federal use.

Criteria

24 CFR 85.32(d) (1) states that property records must be maintained that include a description of the property, a serial number or other identification number, the source of property, who holds the title, the acquisition date, and cost of the property, percentage of Federal participation in the cost of the property, the location and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property

Effects

The lack of proper internal control procedures result in noncompliance with Federal regulations, which may expose the Municipality to cost disallowances by the federal awarding agency. Additionally, the continued occurrence of this situation may result in the misappropriation of assets acquired with federal funds.

Cause

The Municipality has inadequate internal control procedures to prepare and record transactions in the fixed assets subsidiary ledger.

Questioned Costs

None.

Recommendation

The Property Division must require each office, department and federal program that acquires property and equipment to submit a report including a full description of the asset, location, use, responsible personnel, cost and any other pertinent data required by Federal regulations. This information should be reconciled with the monthly disbursements made against the budgetary accounts used for property acquisitions. Sales or other dispositions must also be made only upon approval of the Property Division Director and the Finance Director, and should be carried out by persons other than the users, and through public announcement or bids.

In addition, the Accounting Department should establish a property control account to provide for the reconciliation of property recorded in the subsidiary ledger with that recorded in the control account. In addition, the subsidiary ledger shall be periodically reconciled with the property subsidiary ledgers maintained by the Municipality's several individual federal offices.

Views of Responsible Officials

Management agrees.

Finding Number 05-30

Federal program

Home Investment Partnership Program, CFDA # 14.239

Category

Compliance

Compliance requirements

Allowable Activities

Condition

The Municipality awarded a contract for housing units not affordable to participants. During 2001, the Municipality awarded a contractor \$2,500,000 for the construction of housing units to be made available to low-income families for homebuying upon completion. The project was for 96 one-bedroom apartments convertible to two or three bedrooms, at the cost of the homebuyer. Upon completion of the project, the Municipality could not use 95 of the 96 apartments as the selling price of the units did not make them affordable to low-income families.

The Municipality requested the reimbursement of the full amount awarded to the contractor, but has not required the contractor to pay interest on the amount granted to them since the funds were granted from November 2002 to August 2003. In addition, the Municipality has not taken any sanctions against the contractor, including requesting the federal agencies to suspend or debar the contractor for federal awards.

Funds were returned by the developed through various dates from June 2005 to March 2006. Funds were returned to HUD by the Municipality in late March 2006.

Criteria

24 CFR 92.250(b) states that, before committing funds to a project, the participating jurisdiction must evaluate the project in accordance with guidelines that it has adopted for this purpose and will not invest any more HOME funds, in combination with other governmental assistance, than is necessary to provide affordable housing.

Effects

Payment for non-affordable project may result in cost disallowances by the federal government. In addition interest may be assessed by HUD on funds returned by the developer to the Municipality and not remitted promptly to the federal agency.

Cause

The Municipality entered into housing units construction contracts without first performing an adequate analysis to verify if the units were affordable to lower income homebuyers.

Questioned Costs

None.

Recommendation

The contractor must reimburse the federal program the amount owed as soon as possible. In addition, the Municipality should request the contractor to make interest payments for the amount awarded.

Finally, policies and procedures over project analysis should be restructured to ensure prospectively to ensure that this situation is not repeated. For current projects under construction, the Municipality should perform a subsidy layering analysis with updated data to ensure that if a similar situation is in progress, it is timely detected and corrective actions are taken.

Views of Responsible Officials

Management agrees.

Finding Number 05-31

Federal program

Home Investment Partnership Program, CFDA #14.239

Category

Compliance / Internal Control

Compliance requirement

Eligibility

Earmarking

Specials tests and provisions – Housing quality standards

Condition

The Municipality of San Juan lacks internal controls over tenant-based rental projects assisted with HOME funds. The Municipality awarded on prior year rental-based assistance to various developers for the construction of rental housing projects, which are currently under the period of affordability timeframe. Once the projects were completed, these units have been occupied by participants of the Section 8 and HOPWA programs receiving rental assistance from these two programs.

The following instances of noncompliance were noted:

- HAP calculated for current tenants of these projects are calculated based on rental guidelines and regulations of the HOPWA and Section 8 programs, which are generally higher than those of HOME. This results in current tenants receiving rental assistance in excess of what is allowed for this program.
- The Municipality is not performing the required on-site inspection to the tenant-based rental projects to determine compliance with property standards and housing quality standards. The Municipality is also not verifying the information submitted by the owners.
- The Municipality does not have records of participants who lives on tenant-based rental projects originally assisted through HOME funds. Due to this, we were unable to determine that the subsidized rental units were provided to participants whose income do not exceed 60 percent of the median family income for the area.

Criteria

24 CFR 92.252 required HOME-assisted units in a rental housing project to be occupied only by households that are eligible as low income families and must meet the following requirements to qualify as affordable housing, among others:

- *Rent limitation.* The maximum HOME rents are the lesser of: (a) the fair market rent for existing housing for comparable units in the area as established by HUD under 24 CFR 888.111; or (b) a rent that does not exceed 30 percent of the adjusted income of a family whose annual income equals 65 percent of the median income for the area, as determined by HUD, with adjustments for number of bedrooms in the unit. Additional rent limitations are required for rental projects with five or more HOME-assisted rental units.

- *Tenant income.* The income of each tenant must be determined initially in accordance with 24 CFR 92.203(a)(1)(i). In addition, each year during the period of affordability the project owner must re-examine each tenant's annual income in accordance with one of the options in 24 CFR 92.203 selected by the participating jurisdiction. Additional income provisions are included in 24 CFR 92.252(h).

24 CFR 92.504(d) requires that for HOME assisted rental housing, during the period of affordability the participating jurisdiction must perform on-site inspections of HOME-assisted rental housing to determine compliance with the property standards of 24 CFR 92.251 and to verify the information submitted by the owners in accordance with the requirements of 24 CFR 92.252 no less than: every three years for projects containing 1 to 4 units; every two years for projects containing 5 to 25 units; and every year for projects containing 26 or more units. Inspections must be based on a sufficient sample of units.

24 CFR 92.216 also states that each participating jurisdiction must invest HOME funds made available during a fiscal year so that, with respect to tenant-based rental assistance and rental units, not less than 90 percent of: (a) The families receiving such rental assistance are families whose annual incomes do not exceed 60 percent of the median family income for the area, as determined and made available by HUD with adjustments for smaller and larger families (except that HUD may establish income ceilings higher or lower than 60 percent of the median for the area on the basis of HUD's findings that such variations are necessary because of prevailing levels of construction cost or fair market rent, or unusually high or low family income) at the time of occupancy or at the time funds are invested, whichever is later; or (b) the dwelling units assisted with such funds are occupied by families having such incomes.

Effects

The lack of proper internal control procedures results in noncompliance with Federal regulations, which may expose the Municipality to cost disallowances by the federal awarding agency.

Cause

The Municipality did not consider HOME provisions for rental based assistance projects when tenant based assistance was provided by other federal programs.

Questioned Costs

None.

Recommendation

The Municipality should adopt internal controls and procedures to ensure the compliance with tenant based rental assistance projects.

Views of Responsible Officials

Management agrees.

MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005

COMMUNITY DEVELOPMENT BLOCK GRANT - CFDA # 14.218

The primary objective of the Community Development Block Grant ("CDBG") Entitlement Program (large cities) (24 CFR part 570 subpart D) and HUD-Administered Small Cities Programs (24 CFR part 570 subpart F) is to develop viable urban communities by providing decent housing, a suitable living environment and expanding economic opportunities, principally for persons of low and moderate income.

No audit findings were noted during the current year.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

HIV EMERGENCY RELIEF PROJECT GRANTS – CFDA # 93.914

The objective of this program is to improve access to a comprehensive continuum of high-quality community-based primary medical care and support services in metropolitan areas that are disproportionately affected by the incidence of Human Immunodeficiency Virus (“HIV”)/Acquired Immunodeficiency Syndrome (“AIDS”). The statute refers to both persons infected with HIV and those who have clinically defined AIDS.

Emergency financial assistance, in the form of formula-based funding and supplemental project-based funding, is provided to eligible metropolitan areas (“EMAs”) to develop, organize, and operate health and support services programs for infected individuals and their caregivers. The supplemental grants are discretionary awards and are awarded, following competition, to EMAs that demonstrate severe need beyond that met through the formula award. They must also demonstrate the ability to use the supplemental amounts quickly and cost-effectively. Other criteria, contained in annual application guidance documents, may also apply. All EMAs currently receiving formula assistance are also receiving supplemental assistance.

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

Finding Number 05-32

Federal program

HIV Emergency Relief Project Grants, CFDA # 93.914

Category

Compliance / Internal Control

Compliance requirement

Equipment and Real Property Management

Condition

The Municipality is not maintaining adequate controls over property and equipment items acquired with federal funds. In testing compliance and internal controls over compliance with the equipment and real property management requirement, the following deficiencies were noted:

- The property and equipment records provided did not contain cost nor were properly identified as to whether the assets were acquired with federal funds. Additionally, if any items were acquired in part with Federal funds, property records did not indicate the percentage of Federal participation in the cost of this property.
- Property records could not be reconciled with general ledger amounts.
- There are no established procedures or controls to ensure an immediate update of property records when an item of property or equipment is acquired.

Criteria

45 CFR 92.32 states that property records must be maintained and include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date, and cost of the property, percentage of Federal participation in the cost of the property, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property.

Effects

The lack of proper internal control procedures result in noncompliance with Federal regulations, which may expose the Municipality to cost disallowances by the federal awarding agency. Additionally, the continued occurrence of this situation may result in the misappropriation of assets acquired with federal funds.

Cause

The Municipality has inadequate internal control procedures to prepare and record transactions in the fixed assets subsidiary ledger.

Questioned Costs

None.

Recommendation

The Property Division must require each office, department and federal program that acquires property and equipment to submit a report including a full description of the asset, location, use, responsible personnel, cost and any other pertinent data required by Federal regulations. This information should be reconciled with the monthly disbursements made against the budgetary accounts used for property acquisitions. Sales or other dispositions must also be made only upon approval of the Property Division Director and the Finance Director, and should be carried out by persons other than the users, and through public announcement or bids.

In addition, the Accounting Department should establish a property control account to provide for the reconciliation of property recorded in the subsidiary ledger with that recorded in the control account. In addition, the subsidiary ledger shall be periodically reconciled with the property subsidiary ledgers maintained by the Municipality's several individual federal offices.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

WORKFORCE INVESTMENT ACT (WIA) – CFDA# 17.258, #17.259, #17.260

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

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

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

Finding Number 05-33

Federal program

Workforce Investment Act (WIA) – CFDA # 17.258, # 17.259, # 17.260

Category

Internal Control/ Compliance

Compliance requirements

Reporting

Condition

The cumulative financial reports submitted to the Puerto Rico Human Resources and Occupational Development Council (“PRHRODC”) (do not agree with the accounting records. In addition, the Program does not timely reconcile differences between the Program’s financial monthly reports and the Municipality’s accounting records.

Criteria

Based on provisions of contract agreement between the PRHRODC and the Municipality, the WIA Program of the Municipality is required to submit to the PRHRODC a monthly cumulative expenditure report and is also required to maintain adequate fund accounting.

In addition, OMB Circular A-102, accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or sub grant.

Effects

Failure to report accurate information prevents the granting agency from monitoring the performance of the program’s financial activities, assessing the achievements of the program and evaluating the expected grant award for the following years. At the same time, the Municipality could be exposed to significant adjustments to the grant already awarded.

Cause

As per the Municipality’s management, this report was prepared with the financial data recorded in the books at the program level due to unreconciled differences between the numbers kept at the program level and the numbers in the Municipality’s general ledger. Differences are due to certain expenditures that were recorded by the program but not yet recorded by the Municipality.

Questioned Costs

None.

Recommendation

We recommend that adequate accounting records be developed to provide current, complete, and accurate data. It must include a general ledger and other records such as subsidiary ledgers.

In addition, the Municipality should perform timely reconciliation and cutoff procedures between numbers kept at the federal programs and numbers recorded in the Municipality’s general ledger in order to provide reasonable assurance that financial reports submitted to the federal awarding agency include all activities of the reporting period, are supported by underlying accounting or performance records, and are fairly presented in accordance with program requirements.

Views of Responsible Officials

Management agrees.

Finding Number 05-34

Federal program

Workforce Investment Act (WIA) – CFDA # 17.258, # 17.259, # 17.260

Category

Internal Control/ Compliance

Compliance requirements

Equipment and Real Property Management

Condition

The Municipality is not maintaining adequate controls over property and equipment items acquired with federal funds. In testing compliance and internal controls over compliance with the equipment and real property management requirement, the following deficiencies were noted:

- Property records could not be reconciled with general ledger amounts.
- There are no established procedures or controls that ensure an immediate update of property records when an item of property or equipment is either transferred from one location to another or is disposed of. Without this information the Municipality does not know if it is responsible for compensating the corresponding Federal awarding agencies for their share of any property sold or converted to non-federal use.

Criteria

29 CFR 97.32 states that property records must be maintained and include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date, and cost of the property, percentage of Federal participation in the cost of the property, the location use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property.

Effects

The lack of proper internal control procedures result in noncompliance with Federal regulations, which may expose the Municipality to cost disallowances by the federal awarding agency. Additionally, the continued occurrence of this situation may result in the misappropriation of assets acquired with federal funds.

Cause

The Municipality has inadequate internal control procedures to prepare and record transactions in the fixed assets subsidiary ledger.

Questioned Costs

None.

Recommendation

The Property Division must require each office, department and federal program that acquires property and equipment to submit a report including a full description of the asset, location, use, responsible personnel, cost and any other pertinent data required by Federal regulations. This information should be reconciled with the monthly disbursements made against the budgetary accounts used for property acquisitions. Sales or other dispositions must also be made only upon approval of the Property Division Director and the Finance Director, and should be carried out by persons other than the users, and through public announcement or bids.

In addition, the Accounting Department should establish a property control account to provide for the reconciliation of property recorded in the subsidiary ledger with that recorded in the control account. In addition, the subsidiary ledger shall be periodically reconciled with the property subsidiary ledgers maintained by the Municipality's several individual federal offices.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

HEAD START - CFDA # 93.600

The objectives for the Head Start and Early Head Start programs is to provide comprehensive health, educational, nutritional, social and other developmental services primarily to economically disadvantaged preschool children, infants and toddlers so that the children will attain school readiness. Parents receive social services and participate in various decisions-making processes related to the operation of the program.

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

Finding Number 05-35

Federal program

Head Start, CFDA # 93.600

Category

Compliance / Internal Control

Compliance requirement

Equipment and Real Property Management

Condition

The Municipality is not maintaining adequate controls over property and equipment items acquired by the Head Start Program.

In testing compliance and internal controls over compliance with the equipment and real property management requirement, the following deficiencies were noted:

- The property and equipment records maintained by the Municipality did not provide for the inclusion of the following information: property condition, acquisition cost, percentage of Federal share in acquisition cost, disposal date, and sales price upon disposal. In addition, although location of equipment was included as part of the property records, in some cases the location description is vague or general to determine the exact location of the property acquired.
- The Head Start program has not performed a physical inventory of equipment in the last two years.
- Property records could not be reconciled with general ledger amounts.
- There are no established procedures or controls that ensure an immediate update of property records when an item of property or equipment is acquired. We selected 14 purchases made during FY 2004-05 and noted that for 12 of them (86%) the property records did not include those items.

Criteria

45 CFR 74.30(f) states that equipment records of program's recipients shall include the following information, among others: (a) Acquisition date (or date received, if the equipment was furnished by the Federal Government) and cost; (b) information useful to calculate the percentage of Federal share in the cost of the equipment (not applicable to equipment furnished by the Federal Government); (c) location and condition of the equipment and the date the information was reported; (d) unit acquisition cost; and (e) ultimate disposition data, including date of disposal and sales price or the method used to determine current fair market value where a recipient compensates the Federal awarding agency for its share.

In addition, the recipient shall take a physical inventory of equipment and the results reconciled with the equipment records at least once every two years. Any differences between quantities determined by the physical inspection and those shown in the accounting records shall be investigated to determine the causes of the difference. The recipient shall, in connection with the inventory, verify the existence, current utilization, and continued need for the equipment.

Effects

The lack of proper internal control procedures results in noncompliance with Federal regulations, which may expose the Municipality to cost disallowances by the federal awarding agency. Additionally, the continued occurrence of this situation may result in the misappropriation of assets acquired with federal funds

Cause

The Municipality has inadequate internal control procedures to prepare and record transactions in the fixed assets subsidiary ledger.

Questioned Costs

None.

Recommendation

The Property Division must require each office, department and federal program that acquires property and equipment to submit a report including a full description of the asset, location, use, responsible personnel, cost and any other pertinent data required by Federal regulations. This information should be reconciled with the monthly disbursements made against the budgetary accounts used for property acquisitions. Sales or other dispositions must also be made only upon approval of the Property Division Director and the Finance Director, and should be carried out by persons other than the users, and through public announcement or bids.

In addition, the Accounting Department should establish a property control account to provide for the reconciliation of property recorded in the subsidiary ledger with that recorded in the control account.

Views of Responsible Officials

Management agrees.

**MUNICIPALITY OF SAN JUAN, PUERTO RICO
YEAR ENDED JUNE 30, 2005**

**PUBLIC SAFETY PARTNERSHIP AND COMMUNITY POLICING GRANTS, CFDA
#16.710**

The objectives for the Public Safety Partnership and Community Policing Grants programs is to increase police presence and improve cooperative efforts between law enforcement agencies and members of the community; to expand community policing efforts through the use of technology and other innovative strategies; to increase security and reduce violence in our nation's schools; to address crime and disorder problems; and to otherwise enhance public safety.

No audit findings were noted during the current year.

MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART VII

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2005**

MUNICIPALITY OF SAN JUAN, PUERTO RICO

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2005**

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA or Grant Number	Expenditures
<u>Department of Housing and Urban Development (HUD)</u>		
Section 8 Housing Choice Vouchers	14.871	\$ 26,062,299
Community Development Block Grants/Entitlement Grants	14.218	17,906,167
HOME Investment Partnerships Program	14.239	749,474
Housing Opportunities for Persons with AIDS	14.241	7,001,249
Lower Income Housing Assistance Program-Section 8 Moderate Rehabilitation	14.856	3,964,075
Emergency Shelter Grants Program	14.231	649,597
Supportive Housing Program	14.235	1,347,439
Community Development Block Grants-Section 108 Loan Guarantees	14.248	14,859,915
Shelter Plus Care	14.238	<u>139,134</u>
Subtotal		<u>72,679,349</u>
<u>Department of Health and Human Services (HHS)</u>		
Head Start	93.600	24,812,634
HIV Emergency Relief Project Grants	93.914	14,189,585
Substance Abuse and Mental Health Services	93.243	121,499
Health Center Grants for Homeless Populations (HCH)	93.151	323,264
Pass-through from Commonwealth of Puerto Rico Families and Child Administration—		
Community Services Block Grant	93.569	4,341,644
Pass-through from Commonwealth of Puerto Rico Department of Education—		
Child Care and Development Block Grant (CCDF)	93.575	646
Pass-through from Commonwealth of Puerto Rico Governor's Office—		
Special Programs for the Aging-Title III, Part C-Nutrition Services	93.045	736,017
Pass-through from Commonwealth of Puerto Rico-WESTAT—		
National Health Institute-WESTAT	93.990	649,656
Pass-through from Commonwealth of Puerto Rico Department of Health:		
Risk Reduction	93.941	224,469
Childhood Immunization Grants	93.268	46,949
Maternal and Child Health Services Block Grant to the States	93.994	119,238
Mental Health Clinical and Aids Services	93.244	139,783
Strengthening Families Program	93.556	<u>104,617</u>
Subtotal		<u>45,810,001</u>
<u>Department of Labor (DOL)</u>		
Pass-through the Commonwealth of Puerto Rico Right to Employment Administration—		
Workforce Investment Act (WIA)	17.258, 17.259, 17.260	<u>7,204,886</u>
<u>Department of Justice (DOJ)</u>		
Public Safety Partnership and Community Policing Grants (COPS)	16.710	2,361,783
Drug Free Communities Support Program Grants	16.729	569,407
Gang Resistance Education and Training (GREAT)	16.737	74,184
Community Prosecution Project Safe Neighborhoods	16.609	45,150
Pass-through from Commonwealth of Puerto Rico Department of Justice:		
Local Law Enforcement Block Grants Program	16.592	513,163
Crime Victim Assistance	16.575	81,911
Alcohol, Tobacco and Firearms Training Assistance	16.012	<u>25,975</u>
Subtotal		<u>3,671,573</u>
Subtotal programs		<u>\$ 129,365,809</u>

(continued)

MUNICIPALITY OF SAN JUAN, PUERTO RICO

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2005**

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA or Grant Number	Expenditures
Balance forwarded		\$ 129,365,809
<u>Department of Education (ED)</u>		
Federal Pell Grant Program (PELL)	84.063	2,259,508
TRIO Student Support Services	84.042	251,095
Higher Education - Institutional Aid - Strengthening Institutions Program	84.031	390,398
Supplementary Educational Opportunity Grants	84.007	60,579
Minority Science	84.120	100,591
Federal Work-Study Program (FWS)	84.033	52,160
Subtotal		<u>3,114,331</u>
<u>Department of Agriculture (USDA)</u>		
Pass-through from Commonwealth of Puerto Rico Department of Education— Child and Adult Care Food Program (CACFP)	10.558	<u>1,542,293</u>
<u>Corporation for National and Community Service</u>		
Pass-through from Commonwealth of Puerto Rico Department of Health:		
Foster Grandparent Program	94.011	386,621
Retired and Senior Volunteer Program	94.002	56,412
Subtotal		<u>443,033</u>
<u>Department of Homeland Security</u>		
Emergency Management Performance Grants	97.042	15,579
Homeland Security Grant Program	97.067	114,808
Subtotal		<u>130,387</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS		<u>\$ 134,595,853</u>
See notes to Schedule of Expenditures of Federal Awards		(Concluded)

MUNICIPALITY OF SAN JUAN, PUERTO RICO

**NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE 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 San Juan, Puerto Rico (the “Municipality”), and is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements. The Municipality’s government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, which conform to accounting principles generally accepted in the United States of America (“GAAP”) as applicable to governmental units. The accounts of the Municipality are presented 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. Government resources are allocated to and accounted for by individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

A reconciliation of amounts included in the Schedule of Expenditures of Federal Awards to the other governmental funds column in the fund financial statements follows:

Schedule of expenditures of federal awards	\$ 134,595,853
Nonfederal programs included in the special revenue funds	<u>-</u>
Total special revenue funds	134,595,853
Capital projects funds	<u>11,197,207</u>
Other governmental funds column in the fund financial statements	<u>\$ 145,793,060</u>

2. **Catalog of Federal Domestic Assistance (“CFDA”)** numbers are presented for programs for which such numbers are available.
3. **Reporting Entity**—The Municipality, for purposes of the supplementary Schedule of Expenditure of Federal Awards, includes all the funds of the primary government as defined by GASB Statement No. 14, *The Financial Reporting Entity*.
4. **Subrecipients**—Of the federal expenditures presented, the Municipality provided federal awards to subrecipients from the following Federal programs:

Program Title	Federal CFDA No.	Amount Provided
Community Development Block Grants/Entitlement Grants	14.218	2,355,112
Housing Opportunities for Persons with AIDS	14.241	2,455,393
Substance Abuse and Mental Health Services	93.243	23,277
Mental Health Clinical and AIDS Services	93.244	47,115
Community Services Block Grant	93.569	83,098
Head Start	93.600	1,083,966
HIV Emergency Relief Project Grant	93.914	6,427,065
Community Prosecution Project Safe Neighborhoods	16.609	45,000

MUNICIPALITY OF SAN JUAN, PUERTO RICO

PART VIII

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

The following schedule contains the finding number, title, questioned costs and status of each of the findings included in the schedule of findings and questioned costs relative to federal awards for the year ended June 30, 2005 as required by OMB Circular A-133.



MUNICIPALITY OF SAN JUAN, PUERTO RICO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2005

Reference Number	Finding Description	Questioned Costs	Status
Accounting and Finance Department			
04-1	Deficit in the Municipality's general fund at June 30, 2004.	\$ -	Situation still prevails. Refer to Finding 05-01 and related Corrective Action Plan
04-2	The Municipality is not taking the necessary steps to amortize or reduce the accumulated deficit in the general fund, as required by law.	-	Situation still prevails. Refer to Finding 05-02 and related Corrective Action Plan
04-3	The Municipality does not have an effective system to ensure completeness and accuracy of employee files.	-	Corrective Action Plan implemented with positive results.
04-4	The Municipality does not have effective internal controls to ensure that all Municipal employees are being paid within their salary range based on their respective job classifications.	-	Corrective Action Plan implemented with positive results.
04-5	The Municipality is not canceling outstanding checks, which have been outstanding for a period in excess of six months.	-	Situation still prevails. Refer to Finding 05-03 and related Corrective Action Plan
04-6	Bank charges incurred during prior years not properly expensed.	-	Corrective Action Plan implemented with positive results.
04-7	Untimely preparation of financial statements.	-	Corrective Action Plan implemented with positive results.
04-8	Inadequate records for interfund transactions.	-	Corrective Action Plan implemented with positive results.
04-9	Inactive and unnecessary funds and accounts are not closed.	-	Situation still prevails. Refer to Finding 05-04 and related Corrective Action Plan
04-10	The Municipality's payroll register totals are not distributed in accordance with the general ledger accounts.	-	Situation still prevails. Refer to Finding 05-05 and related Corrective Action Plan
04-11	The Municipality does not perform an annual physical inventory.	-	Situation still prevails. Refer to Finding 05-06 and related Corrective Action Plan
04-12	The Municipality does not have procedures in place to verify the status of an entity as to suspension and debarment when contracting services or procuring goods with federal funds.	-	Situation still prevails. Refer to Finding 05-08 and related Corrective Action Plan
Section 8 Housing Choice Vouchers			
04-13	Inadequate documentation of participant files.	63,912	Situation has been corrected in part due to implementation of Corrective Action Plan. Refer to finding 05-12.
04-14	Inadequate controls over participants' records.	30,984	Corrective Action Plan implemented with positive results.
04-15	The Municipality did not ensure that owners of program units failing to meet Housing Quality Standards ("HQS") corrected deficiencies within 30 calendar days or within any specified extension approved by them.	-	Corrective Action Plan implemented with positive results.
04-16	The Municipality did not maintain an up-to-date utility allowance schedule.	-	Situation still prevails. Refer to Finding 05-15 and related Corrective Action Plan
04-17	The Municipality has not reimbursed the federal program for the federal funds used to finance general fund's activities.	777,491	Corrective Action Plan implemented with positive results.
04-18	The Municipality has not collected its accounts receivable.	1,026,034	Situation has been corrected in part due to implementation of Corrective Action Plan. Refer to finding 05-10.



MUNICIPALITY OF SAN JUAN, PUERTO RICO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2005

Reference Number	Finding Description	Questioned Costs	Status
04-19	The Municipality filed HUD Form 52681 with amounts that do not agree with the general ledger.	-	Situation still prevails. Refer to Finding 05-18 and related Corrective Action Plan
04-20	The Municipality is not maintaining adequate controls over property and equipment items acquired by the Section 8 Housing Choice Vouchers Program.	-	Corrective Action Plan implemented with positive results.
04-21	The Municipality is not documenting the rationale used to admit participants from the waiting list.	75,660	Situation still prevails. Refer to Finding 05-16 and related Corrective Action Plan
04-22	The Municipality is removing applicants from the waiting list.	56,568	Corrective Action Plan implemented with positive results.
Lower Income Housing Assistance Program - Section 8 Moderate Rehabilitation			
04-23	The Municipality filed HUD Form 52681 with amounts that do not agree with the general ledger.	-	Situation still prevails. Refer to Finding 05-22 and related Corrective Action Plan
04-24	The Municipality is not maintaining adequate controls over property and equipment items acquired by the Section 8 Moderate Rehabilitation Program.	-	Corrective Action Plan implemented with positive results.
Community Development Block Grant/Entitlement Grants			
04-25	The Municipality does not have adequate controls over property and equipment acquired with federal funds.	-	Corrective Action Plan implemented with positive results.
04-26	A certification from the Municipality's subrecipients indicating that their organizations and its principals were not suspended or debarred was not included in the files.	-	Corrective Action Plan implemented with positive results.
04-27	The Municipality filed the Consolidated Annual Performance Report ("CAPER") with amounts that do not agree with the general ledger.	-	Corrective Action Plan implemented with positive results.
HOME Investment Partnership Program			
04-28	The Municipality's internal control over compliance with the documentation of participant's files is not working effectively.	43,000	Situation has been corrected in part due to implementation of Corrective Action Plan. Refer to finding 05-28.
04-29	The Municipality does not have adequate controls over property and equipment acquired by the HOME program.	-	Situation still prevails. Refer to Finding 05-29 and related Corrective Action Plan
Housing Opportunities for Persons with AIDS			
04-30	The Municipality filed HUD Form 40110 with amounts that do not agree with the general ledger.	-	Situation still prevails. Refer to Finding 05-25 and related Corrective Action Plan
04-31	The Municipality is not maintaining adequate controls over property and equipment items acquired by the HOPWA program.	-	Corrective Action Plan implemented with positive results.



MUNICIPALITY OF SAN JUAN, PUERTO RICO

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2005

Reference Number	Finding Description	Questioned Costs	Status
IIIV Emergency Relief Project Grants			
04-32	The Municipality did not obtain a certification from its subrecipients indicating that their organizations and its principals were not suspended or debarred.	-	Corrective Action Plan implemented with positive results.
04-33	The Municipality does not have proper procedures to assure that grant funds assigned to subgrantees are properly monitored.	-	Corrective Action Plan implemented with positive results.
04-34	The Municipality is not maintaining adequate controls over property and equipment items acquired with federal funds.	-	Situation still prevails. Refer to Finding 05-32 and related Corrective Action Plan
Workforce Investment Act			
04-35	Accounting records do not provide sufficient information to determine compliance with the earmarking requirement.	-	Corrective Action Plan implemented with positive results.
04-36	The cumulative financial reports submitted to the PRHRODC do not agree with the accounting records.	-	Situation still prevails. Refer to Finding 05-33 and related Corrective Action Plan
04-37	The Municipality is not maintaining adequate controls over property and equipment items acquired with federal funds.	-	Situation still prevails. Refer to Finding 05-34 and related Corrective Action Plan
		\$ 2,073,649	