

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

**MUNICIPIO DE SANTA ISABEL
AUDITORÍA 2011-2012
30 DE JUNIO DE 2012**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**



SINGLE AUDIT REPORT

For the Fiscal Year Ended June 30, 2012
(With Independent Auditors' Report Thereon)

Municipality of Santa Isabel, P.O. Box 725, Santa Isabel, Puerto Rico 00757
Hon. Enrique H. Questell Alvarado

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Single Audit Report**

June 30, 2012

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PEDRO C. ORTIZ LEDEE
CERTIFIED PUBLIC ACCOUNTANT

INDEPENDENT AUDITOR'S REPORT

To the Honorable Mayor and
Members of the Municipal Legislature
Municipality of Santa Isabel, 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 **Santa Isabel**, Puerto Rico (Municipality), as of and for the fiscal year ended June 30, 2012, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

The Municipality did not have a complete, updated and accurate accounting records of the capital assets, accumulated depreciation and related depreciation expense and we were unable to satisfy ourselves about such balances through alternate procedures. Therefore, we were unable to obtain sufficient and competent evidential matter related to the capital assets reported in the accompanying statement of net assets for \$22,988,074, net of accumulated depreciation of \$8,873,792 and the amount of depreciation expense stated at \$949,129 reported in the accompanying statement of activities for the year then ended. In addition, the expenses and the net result of operations reported in the accompanying statement of activities are also misstated for amounts that could not be determined for the fiscal year ended June 30, 2012.

We were unable to obtain an evaluation from the Municipality's external lawyers of the pending or threatened litigations as of June 30, 2012, as discussed in note 13 to the financial statements.

The Municipality did not maintain adequate accounting records of the interfund cash transactions and the corresponding due from and due to account balances. We were unable to obtain sufficient evidence to support and satisfy ourselves about the amounts recorded as interfund balances in the amount of \$1,289,219 in each major fund and the aggregate remaining fund in the Balance Sheet of the governmental funds at June 30, 2012.

Because of the significance of the matter discussed in the third and fourth paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial position of the governmental activities of the Municipality at June 30, 2012, and the respective changes in financial position, thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

In addition, in our opinion, except for the effects of such adjustments, if any as might have been determined to be necessary regarding the interfund transactions of each major fund and the aggregate remaining fund information, as described in the fifth paragraph, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major fund, and the aggregate remaining fund information of the Municipality, as of June 30, 2012, and the respective changes in financial position thereof for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 10, 2013, on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and 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.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the budgetary comparison information on pages 3 through 15 and 72 through 74 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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


Pedro C. Ortiz Ledée, CPA
License Number 5200

Guayama, Puerto Rico
July 10, 2013

Stamp Num. 2671582 was affixed
to the original of this report



**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

As management of the Municipality of Santa Isabel (the Municipality), we offer readers the following discussion and analysis of the Municipality's financial activities reported in the accompanying basic financial statements as of and for the fiscal year ended June 30, 2012. We encourage readers to consider the information presented here in conjunction with additional information that is furnished in the accompanying financial statements, which follow this narrative.

Besides, this document includes comparative data with prior year as this information was available for the fiscal year ended on June 30, 2011. This MD&A is prepared in order to comply with the dispositions established in the Governmental Accounting Standards Board (GASB) Statement No. 34, "*Basic Financial Statements – and Management's Discussion and Analysis-for State and Local Governments*" and, among other purposes, to provide the financial statements users with the following major information:

- a broader basis in focusing important issues;
- acknowledgement of an overview of the Municipality's financial activities;
- provides for an evaluation of its financial condition as of the end of fiscal year 2011-2012 compared with prior year results;
- identification of uses of funds in the financing of the Municipality's variety of activities and;
- asses management's ability to handle budgetary functions.

FINANCIAL HIGHLIGHTS

Government-Wide Highlights:

- The Municipality's total assets amounted to \$32,328,713 at June 30, 2012, of which \$22,988,074 consist of capital assets (net of accumulated depreciation and amortization of \$8,873,792), \$1,054,285 consist of cash and cash equivalents, \$6,892,658 consist of cash with fiscal agent (which are restricted principally for capital projects and debt service) and \$1,393,696 consist of accounts receivable.
- The Municipality's total liabilities amounted to \$34,942,623 at June 30, 2012, of which \$23,272,500 consist of bonds and notes payable, \$2,806,456 consist of accounts payable and accrued liabilities, \$2,099,676 consist of intergovernmental payables, \$1,517,183 consist of accrued compensated absences, \$1,235,357 consist of unearned revenues, \$265,969 consist of accrued christmas bonus, \$485,482 consist of accrued interest payable on long-term debt, and \$3,260,000 consist of estimated landfill closure and post closure care costs.
- The Municipality's total liabilities exceeded its assets (net liabilities) by (\$2,613,910) at June 30, 2012.
- The Municipality's total revenues amounted to \$18,313,365 for the fiscal year ended June 30, 2012, of which \$8,794,416 arose from taxes, \$8,517,312 arose from intergovernmental grants and contributions, and \$1,001,637 arose from charges from services, miscellaneous revenues and interest on deposits.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

- The Municipality's total expenses amounted to \$21,284,058 for the fiscal year ended June 30, 2012, of which \$14,112,103 were incurred in providing direct services and benefits to citizens in relation to urban and economic development, health and sanitation, public safety, welfare and housing assistance, culture, recreation and education. In addition, the Municipality incurred in \$903,213 of its total expenses, in interests related to its long-term obligations, and \$6,268,742 in general government activities to support the Municipality's functions and programs. The Municipality's total expenses include depreciation and amortization of capital assets in the amount of \$949,129 for the fiscal year ended June 30, 2012.
- The Municipality's total net assets decreased by \$2,970,693 during the fiscal year ended June 30, 2012.

Governmental Funds' Highlights:

- The total fund balances of governmental funds amounted to \$2,779,905 at June 30, 2012, which are restricted for capital projects, debt service and other specific purposes.
- The governmental funds presented an unassigned fund deficit of (\$4,012,653).
- The fund balances of governmental funds decreased by \$3,297,878 during the fiscal year ended June 30, 2012.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The purpose of financial reporting is to provide external users of basic financial statements with information that will help them to make decisions or draw conclusions about the Municipality. There are many external parties that use the basic financial statements of the Municipality; however, these parties do not always have the same specific objectives. In order to address the needs of as many parties as reasonably possible, the Municipality, in accordance with required financial reporting standards, presents this Management's Discussion and Analysis (MD&A) as an introduction to the accompanying basic financial statements. This narrative represents an overview and analysis of the financial activities of the Municipality for the fiscal year ended June 30, 2012. Because this MD&A is designed to focus on the current year activities, resulting changes and currently known facts, we encourage readers to consider the information presented in this MD&A in conjunction with the additional information furnished in the accompanying basic financial statements.

The Municipality's basic financial statements include three components: (1) government-wide financial statements (GWFS), (2) fund financial statements (FFS), and (3) notes to the basic financial statements (NBFS). This report also contains additional required information in addition to the basic financial statements themselves. These components are described below.

The basic financial statements focus on: (1) the Municipality as a whole (government-wide financial reporting) and, (2) the Municipality's major individual governmental funds. Both perspectives allow the users to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability. The components of the basic financial statements are described below.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

a) Government-Wide Financial Statements

The GWFS are composed of: (1) the statements of net assets (SNA) and (2) the statement of activities (SA). These financial statements can be found immediately following this MD&A. GWFS are designed to provide readers with a broad overview of the Municipality's operations as a whole in a manner similar to private-sector businesses. These statements provide short-term and long-term information about the Municipality's financial position, which assist the Municipality's management to determine the economic condition at June 30, 2012. The GWFS are prepared using methods that are similar to those used by most private businesses.

Both of the government-wide financial statements distinguish functions of the Municipality that are principally supported by taxes and intergovernmental activities (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*).

1. Statement of Net Assets

The purpose of SNA is to attempt to report all assets owned and all liabilities owed by the Municipality. The Municipality reports of all of its assets when it acquires ownership over the assets and reports all of its liabilities when they are incurred. For example, the Municipality reports buildings and infrastructure as assets, even though they are not available to pay the obligations incurred by the Municipality. On the other hand, the Municipality reports liabilities, such as claims and judgments, bonds and notes payable, obligations under capital leases, compensated absences and certain accounts payable and accrued liabilities, even though these liabilities might not be paid until several fiscal years into the future.

The difference between the Municipality's total assets and total liabilities reported in SNA is presented as *net assets*, which is similar to the total owners' equity reported by a commercial enterprise in its financial statements. Although the purpose of the Municipality is not to accumulate net assets, as this amount increases or decreases over time, such amount represents a useful indicator of whether the financial position of the Municipality is either improving or deteriorating, respectively.

2. Statement of Activities

The SA presents information showing how the Municipality's net assets changed during the fiscal year ended June 30, 2012, by presenting all of the Municipality's revenues and expenses. As previously discussed, the items reported in SA are measured in a manner similar to the approach used by a commercial enterprise in that revenues are recognized when earned or established criteria are satisfied, and expenses are recorded when incurred by the Municipality. Consequently, revenues are reported even when they may not be collected for several months after the end of the fiscal year and expenses are recorded even though they may not have used cash during the current year.

Although SA looks different from a commercial enterprise's income statement, the difference is only in format, not substance. Whereas the bottom line in a commercial enterprise represents its net income, the Municipality reports an amount described as *net change in net assets*, which is essentially the same concept.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

The focus of SA is on the *net cost* of various activities provided by the Municipality. The statement begins with a column that identifies the cost of each of the Municipality's major functions. Another column identifies the revenues that are specifically related to the classified governmental functions. The difference between the expenses and revenues related to specific functions/programs identifies the extent to which each function of the Municipality draws from general revenues or is self-financing through fees, intergovernmental aid, and other sources of resources.

This statement also presents a comparison between direct expenses and program revenues for each function of the Municipality.

GWFS and FFS present all of the Municipality's governmental activities, which are supported mostly by taxes, intergovernmental revenues (such as federal and state grants and contributions), and charge for services. All services normally associated with the Municipality fall into this category, including culture, recreation and education; general government; health and sanitation; public safety; welfare and housing assistance; and urban and economic development.

b) Fund Financial Statements

The Municipality's FFS consist of: (1) the balance sheet – governmental funds and (2) the statement of revenues, expenditures and changes in fund balances – governmental funds. These financial statements report the financial position, the results of operations of the Municipality's governmental funds, with an emphasis on the Municipality's major governmental funds.

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Municipality, like most other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. Each fund is considered an independent fiscal entity accounted for within a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenue, and expenditures. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial and contractual provisions. All of the funds of the Municipality can be divided into two categories: governmental funds and proprietary funds.

1. Governmental funds

Governmental funds are used to account for most of the services provided by the Municipality. These funds are used to account for essentially the same functions reported as governmental activities in the GWFS. Unlike GWFS, the focus of governmental funds in the FFS is directed to specific activities of the Municipality rather than the Municipality as a whole; therefore, governmental funds in FFS report the Municipality's operations in more detail than the GWFS.

Governmental funds in FFS provide a detailed short-term view of the Municipality's finances that assist in determining whether there will be adequate financial resources available to meet the current needs of the Municipality, which is, evaluating the Municipality's near-term financing requirements. For financial reporting purposes, the Municipality classifies its governmental funds within the following types: (1) general fund, (2) debt service fund, (3) special revenue funds, (4) capital projects funds and (5) permanent funds.

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Governmental funds FFS are prepared on an accounting basis that is significantly different from that used to prepare GWFS. In general, governmental funds FFS focus on near-term inflows and outflows of expendable financial resources, consequently, they measure and account for cash and other assets that can easily be converted to cash. For example, amounts reported on the balance sheet include capital assets within a very short period of time, but do not include capital assets such as land and buildings. Governmental fund liabilities generally include amounts that normally are going to be paid within a short period after the end of the fiscal year. The difference between a fund's total assets and total liabilities is reported as the fund balance or deficit, and generally indicates the amount that can be used to finance the next fiscal year's activities. Likewise, the operating statement for governmental funds reports only those revenues and expenditures that were collected in cash or paid with cash, respectively, during the current fiscal year or very shortly after the end of the fiscal year.

Because the focus of governmental funds FFS is narrower than that of the GWFS, it is useful to compare the fund information presented for governmental funds with similar information presented for governmental activities in the GWFS. By doing so, readers may better understand the long-term impact of the Municipality's near-term financial decisions. Both the governmental funds' balance sheet and the governmental funds' statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate the comparison between governmental funds and the governmental activities reported in the government-wide financial statements.

The Municipality has four major governmental funds. Each major fund is presented in a separate column in the balance sheet – governmental funds and the statement of revenues, expenditures and changes in fund balances – governmental funds. The four major governmental funds are: (1) general fund, (2) state legislative joint resolutions fund, (3) capital improvement bond fund and (4) debt service fund.

c) Notes to Basic Financial Statements

The NBFS provide additional information that is essential for a full understanding of the data provided in the GWFS and FFS. The NBFS can be found immediately following the basic financial statements.

d) Other Supplementary Information

The basic financial statements are followed by a section of other supplementary information consisting of budgetary comparison schedule – general fund.

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**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

FINANCIAL ANALYSIS OF GOVERNMENT-WIDE FINANCIAL STATEMENTS

The Municipality's overall financial position and operations at June 30, 2012 and 2011 are summarized as follows, based on the information included in the accompanying statement of net assets:

	<u>Governmental activities</u>		<u>Change</u>	
	<u>2012</u>	<u>2011</u>	<u>\$</u>	<u>%</u>
<i>Assets:</i>				
Current assets	\$9,340,639	\$13,300,812	\$(3,960,173)	(30%)
Non-current assets:				
Capital assets, net	22,988,074	23,633,249	(645,175)	(3%)
Total assets	<u>32,328,713</u>	<u>36,934,061</u>	<u>(4,605,348)</u>	<u>(33%)</u>
<i>Liabilities:</i>				
Current liabilities, excluding long-term obligations	5,444,818	6,310,160	(865,342)	(14%)
Long-term obligations:				
Due within one year	3,176,064	3,278,830	(102,766)	(3%)
Due after one year	26,321,741	26,988,288	(666,547)	(2%)
Total liabilities	<u>34,942,623</u>	<u>36,577,278</u>	<u>(1,634,655)</u>	<u>(19%)</u>
<i>Net assets (deficit):</i>				
Invested in capital assets, net of related debt	17,680,009	19,692,926	(2,012,917)	(10%)
Restricted	5,726,377	3,851,497	1,874,880	49%
Unrestricted	(26,020,296)	(23,187,640)	(2,832,656)	12%
Total net assets	<u>\$(2,613,910)</u>	<u>\$ 356,783</u>	<u>\$(2,970,693)</u>	<u>51%</u>

At June 30, 2012, the Municipality's current assets, amounting to \$9,340,639 are mainly composed of restricted and unrestricted cash and cash equivalents (\$1,054,285), restricted cash with fiscal agent (\$6,892,658), and restricted and unrestricted intergovernmental grants and contributions receivable (\$1,103,107).

The restricted cash represents resources legally designated for: (1) the payment of debt service, (2) the acquisition, construction and improvement of major capital assets, and (3) the operations of federally and state funded grant programs. Restricted cash also consists of unspent proceeds of bonds issued for acquisition, construction and improvement of major capital assets, and to pay operational debts.

The Municipality's non-current assets, amounting to \$22,988,074 at June 30, 2012, are substantially composed of capital assets, with a cost basis of \$31,861,866, which are reported net of accumulated depreciation and amortization of \$8,873,792.

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Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

At June 30, 2012, the Municipality's current liabilities (excluding current portion of long-term liabilities) amounting to \$5,444,818 are mainly composed of unearned revenues (\$1,235,357), accounts payable and accrued liabilities (\$2,806,456), and intergovernmental payables (\$917,523). Unearned revenues principally consist of unearned revenues associated with municipal license taxes and intergovernmental grants and contributions related to state and federally funded grant programs.

The Municipality's non-current liabilities, amounting to \$29,497,805 at June 30, 2012, are mainly composed of current portion and the portion due after one year of bonds and notes payable (\$23,272,500).

As noted earlier, net assets may serve over time as a useful indicator of the Municipality's financial position. The liabilities of the Municipality exceeded assets by (\$2,613,910) at June 30, 2012. The most significant portion of net assets (\$17,680,009) reflects the Municipality's investment in capital assets (e.g. land, buildings, machinery, equipment, furniture, fixtures, infrastructure, etc.), net of all related debt still outstanding that was issued to acquire, construct or improve 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 capital assets is reported net of the outstanding related debt, the resources needed to repay that debt must be provided by other sources, since capital assets cannot be used to liquidate these liabilities.

Another significant portion of net assets at June 30, 2012, represents resources that are restricted for debt service payments (\$4,356,602) and for other specified purposes (\$1,369,775).

The remaining component of total net assets consists of unrestricted net liabilities amounting to (\$26,020,296) at June 30, 2012. These unrestricted net liabilities are the consequence of previous budgets that did not provide sufficient funding for incurred long-term obligations, such as bonds and notes payable, compensated absences, etc. Historically, a significant portion of such obligations has been budgeted on a pay-as-you-go basis.

The total net assets of the Municipality decreased by \$2,970,693 for the fiscal year ended June 30, 2012. Such decrease is due to the excess of total expenses (\$21,284,058), including depreciation and amortization of capital assets of (\$949,129), over total revenues (\$18,313,365) for the fiscal year ended June 30, 2012.

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**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

The following is a condensed presentation of the Municipality's results of operations as reported in the statement of activities for the fiscal years ended June 30, 2012 and 2011:

	Governmental activities		Change	
	2012	2011	\$	%
Program revenues:				
Program-specific operating grants and contributions	\$ 1,333,386	\$ 1,602,081	\$ (268,695)	(17%)
Program-specific capital grants and contributions	2,373,726	1,323,650	1,050,076	79%
Charges for services	674,180	60,081	614,099	1022%
Total program revenues	<u>4,381,292</u>	<u>2,985,812</u>	<u>1,395,480</u>	<u>1085%</u>
General revenues:				
Property taxes	4,178,828	3,477,671	701,157	20%
Municipal license taxes	1,610,585	1,353,231	257,354	19%
Sales and use taxes	748,521	461,001	287,520	62%
Construction excise taxes	2,256,482	2,030,288	226,194	11%
Unrestricted grants and contributions	4,810,200	4,344,457	465,743	11%
Other general revenues (various sources)	327,457	491,914	(164,457)	(33%)
Total general revenues	<u>13,932,073</u>	<u>12,158,562</u>	<u>1,773,511</u>	<u>90%</u>
Total revenues	<u>18,313,365</u>	<u>15,144,374</u>	<u>3,168,991</u>	<u>1175%</u>
Program expenses:				
General government	6,268,742	3,626,602	2,642,140	73%
Urban and economic development	9,913,526	7,473,449	2,440,077	33%
Public safety	715,630	805,013	(89,383)	(11%)
Health and sanitation	922,443	2,568,527	(1,646,084)	(64%)
Culture, recreation and education	1,599,189	1,652,883	(53,694)	(3%)
Welfare and housing assistance	961,315	1,035,350	(74,035)	(7%)
Interest on long-term obligations	903,213	773,006	130,207	17%
Total expenses	<u>21,284,058</u>	<u>17,934,830</u>	<u>3,349,228</u>	<u>37%</u>
Net increase (decrease) in net assets	(2,970,693)	(2,790,456)	(180,237)	1138%
Net assets, at beginning of fiscal year, as restated	356,783	3,147,239	(2,790,456)	(89%)
Net assets, at end of fiscal year	<u>\$(2,613,910)</u>	<u>\$ 356,783</u>	<u>\$(2,970,693)</u>	<u>1049%</u>

As previously mentioned, the Municipality's total net assets decreased by \$2,970,693 during the current fiscal year. Approximately 48% (\$8,794,416) of the Municipality's total revenues for the current fiscal year came from property, municipal license, construction excise and sales and use taxes, while 47% (\$8,517,312) resulted from restricted and unrestricted capital and operating grants and contributions. Charges for services and other revenues, amounting to \$1,001,637, provided 5% of the total revenues for the current fiscal year.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

The Municipality's expenses cover a wide range of services. The largest expenses of the Municipality for the fiscal year ended June 30, 2012 were related to: (1) general administrative and operating costs (\$6,268,742), which were classified as "general government" and accounted for 29% of total expenses, (2) welfare and housing assistance (\$961,315), which accounted for 5% of total expenses, (3) health and sanitation (\$922,443), which accounted for 4% of total expenses, (4) urban and economic development (\$9,913,526), which accounted for 47% of total expenses, (5) public safety (\$715,630), which accounted for 3% of total expenses, (6) culture, recreation and education (\$1,599,189), which accounted for 8% of total expenses, and (7) interest on long-term obligations (\$903,213), which accounted for 4% of total expenses. These expenses include depreciation of capital assets and deferred charges in the amount of \$949,129, for the fiscal year ended June 30, 2012.

FINANCIAL ANALYSIS OF GOVERNMENTAL ACTIVITIES

Analysis of Financial Position of Governmental Funds

As discussed earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of expendable resources. Such information is useful in assessing the Municipality's compliance with finance-related legal requirements. Specifically, unreserved fund balance may serve as a useful measure of the Municipality's net resources available for spending at the end of the fiscal year.

At June 30, 2012, the total assets of governmental funds amounted to \$10,629,858, which consisted of: (1) cash and cash equivalents of \$1,054,285; (2) cash in fiscal agent of \$6,892,658; (3) Due from other funds of \$1,289,219, and; (4) property and sales taxes, intergovernmental, accrued interests and other receivables of \$1,393,696. Such assets include cash, cash equivalents and receivables that are principally used for debt service, capital projects and other specific purposes.

At June 30, 2012, the total liabilities of governmental funds amounted to \$7,849,953, which consisted of: (1) deferred revenues of \$1,796,273; (2) accounts payable and accrued liabilities of \$2,806,456; (3) intergovernmental accounts payable of \$917,523; (4) Due to other funds of \$1,289,219, and; (5) matured bonds and interests due and payable of \$1,040,482.

The total fund balances of governmental funds amounted to \$2,779,905 at June 30, 2012, which are restricted for capital projects, debt service and other specific purposes. The fund balances of governmental funds decreased by \$3,297,878 during the fiscal year ended June 30, 2012.

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**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

The following table presents the condensed financial position of governmental funds at June 30, 2012 and 2011:

	2012	2011
Assets:		
Total assets - major governmental funds	\$ 9,540,957	\$ 12,313,816
Total assets - other governmental funds	1,088,901	2,814,319
Combined total assets	10,629,858	15,128,135
Liabilities:		
Total liabilities - major governmental funds	6,949,034	7,534,379
Total liabilities - other governmental funds	900,919	1,515,973
Combined total liabilities	7,849,953	9,050,352
Fund balances (deficits):		
Restricted, Committed or Assigned – Major Funds	6,604,576	5,614,455
Restricted, Committed or Assigned – Other Funds	187,982	1,298,346
Unassigned	(4,012,653)	(835,018)
Combined total fund balances	2,779,905	6,077,783
Total liabilities and fund balances	\$ 10,629,858	\$ 15,128,135

Major Governmental Funds

General fund (GF) – The GF is the principal operating fund of the Municipality. The GF's total assets amounted to \$1,505,132 at June 30, 2012. Such assets consist principally of: (1) Cash in commercial banks (\$359,560), (2) sales and use tax receivables (\$130,116), (3) short-term amounts due from other funds (\$204,045), (4) due from governmental entities (\$560,916), and (5) restricted cash in fiscal agent (\$221,014).

The GF's total liabilities amounted to \$5,406,039 at June 30, 2012. Such liabilities are composed of: (1) deferred revenues (\$1,618,522), (2) due to other funds (\$1,084,769), and (2) accounts payable and accrued liabilities, including amounts due to other governments (\$2,702,748).

At the end of the current fiscal year, restricted fund balance amounted to \$111,746 and unassigned fund deficit amounted to (\$4,012,653).

State legislative joint resolutions fund (SLJRF)- The SLJRF's total assets amounted to \$1,389,300 at June 30, 2012, which consist of : (1) cash in commercial banks (\$334,605), and (2) due from other funds (\$1,054,695). The SLJRF's total liabilities amounted to \$207,507 at June 30, 2012, which are composed of accounts payable and accrued liabilities. At the end of the current fiscal year, the SLJRF had total restricted fund balances amounted to \$1,181,793.

**MUNICIPALITY OF SANTA ISABEL,
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Management's Discussion and Analysis
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Capital improvement bond fund (CIBF)- The CIBF's total assets amounted to \$1,804,441 at June 30, 2012, which consist of restricted cash with fiscal agent. The CIBF's total liabilities amounted to \$295,006 at June 30, 2012, which are composed of accounts payable and accrued liabilities. At the end of the current fiscal year, the CIBF had total restricted fund balances amounted to \$1,509,435.

Debt service fund (DSF)- The DSF's total assets amounted to \$4,842,084 at June 30, 2012, which consist mainly of restricted cash in fiscal agent (\$4,738,674). The DSF's total liabilities amounted to \$1,040,482 at June 30, 2012, which are composed of: (1) matured bonds due and payable (\$555,000), and (2) matured interest due and payable (\$485,482). At the end of the current fiscal year, DSF's total and restricted fund balance amounted to \$3,801,602.

Other governmental funds (OGF)- The OGF's total assets amounted to \$1,088,901 at June 30, 2012, which consist mainly of restricted cash and cash equivalents (\$360,120), cash in fiscal agent (\$128,529), due from other governmental funds (\$30,479), and receivables from intergovernmental grants and contributions (\$542,191). The OGF's total liabilities amounted to \$900,919 at June 30, 2012, which are composed of deferred revenues (\$177,751), accounts payable and accrued liabilities (\$518,718) and short-term amounts due to other funds (\$204,450). At the end of the current fiscal year, OGF's total restricted fund balance amounted to \$187,982.

Analysis of Operating Results of Governmental Funds

Major Governmental Funds

General fund – The total fund deficit of the GF increased by (\$3,532,016) during current fiscal year. Total revenues, expenditures and other financing sources (net) amounted to \$11,231,434, \$14,581,463, and (\$181,987), respectively, for the fiscal year ended June 30, 2012.

Approximately 54% (\$6,073,180) of the GF's total revenues for the current fiscal year came from property, municipal license, construction excise and sales and use taxes, while 43% (\$4,796,824) resulted from intergovernmental grants and contributions. Interest revenues, charges for services and miscellaneous revenues, amounting to \$361,430, provided 3% of the total revenues for the current fiscal year.

The largest expenses of the GF for the fiscal year ended June 30, 2012 were related to: (1) general administrative and operating costs (\$6,091,041), which were classified as "general government" and accounted for 42% of total expenses, (2) welfare and housing assistance (\$470,978), which accounted for 3% percent of total expenses, (3) health and sanitation (\$547,435), which accounted for 4% of total expenses, (4) urban and economic development (\$6,245,883), which accounted for 43% of total expenses, (5) public safety (\$518,517), which accounted for 3% of total expenses, and (6) culture, recreation and education (\$707,609), which accounted for 5% of total expenses.

State legislative joint resolutions fund (SLJRF)- The total fund balance of the SLJRF decreased by \$19,052 during current fiscal year. Total expenditures amounted to \$644,874 for the fiscal year ended June 30, 2012.

SLJRF's total expenditures for the current fiscal year came from urban and economic development.

**MUNICIPALITY OF SANTA ISABEL,
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Management's Discussion and Analysis
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Capital improvement bond fund (CIBF)- The total fund balance of the CIBF decreased by \$1,068,569 during current fiscal year. Total expenditures amounted to \$1,068,569 for the fiscal year ended June 30, 2012.

CIBF's total expenditures for the current fiscal year came from urban and economic development.

Debt service fund (DSF) – The total fund balance of the DSF increased by \$1,231,278 during current fiscal year. Total revenues, expenditures and other financing sources (net) amounted to \$2,565,504, \$1,516,213 and \$181,987, respectively, for the fiscal year ended June 30, 2012.

Approximately 69% (\$1,776,816) of DSF's total revenues for the current fiscal year came from restricted property taxes, while 31% (\$787,436) came from restricted sales and use taxes. DSF's total expenditures for the current fiscal year came from principal and interests on bonds payable (\$1,516,213).

Other governmental funds (OGF) – The total fund balance of the OGF increased by \$90,481 during current fiscal year. Total revenues and expenditures amounted to \$3,688,558 and \$3,598,077, respectively, for the fiscal year ended June 30, 2012. Approximately 78% (\$2,863,929) of OGF's total revenues for the current fiscal year came from intergovernmental grants.

The largest expenses of the OGF for the fiscal year ended June 30, 2012 were related mainly to: (1) urban and economic development (\$1,786,821), which accounted for 50% of total expenses, (2) welfare and housing assistance (\$482,812), which accounted for 13% percent of total expenses, (3) health and sanitation (\$530,258), which accounted for 15% of total expenses, and (4) culture, recreation and education (\$680,573), which accounted for 19% of total expenses.

BUDGETARY HIGHLIGHTS

a) General Fund

The original budget of the general fund for the fiscal year ended June 30, 2012 amounted to \$11,504,525. The final budget of the general fund for the fiscal year ended June 30, 2012 amounted to \$12,006,899. Over the course of the fiscal year, the Municipality revised the GF's budget in order to include increases and decreases in expenditures. The laws and regulations of the Commonwealth mandate a balanced budget.

The total actual revenues (budgetary basis) of the general fund for the fiscal year ended June 30, 2012 were \$11,212,559, which is \$794,340 lower than the budgeted revenues. In addition, the total actual expenditures (budgetary basis) of the general fund for the fiscal year ended June 30, 2012 were \$13,801,945, which is \$1,485,057 more than the budgeted expenditures.

The most significant fluctuations in actual revenues occurred in municipal license, construction excise and sales taxes, which had actual revenues that were \$163,382, \$554,379 and \$309,415 lower than budgeted.

Also, the most significant fluctuations in actual expenditures occurred in general government, which had actual expenditures that were \$1,227,241 more than budgeted, and in urban and economic development, which had actual expenditures that were \$668,051 more than budgeted.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2012

CAPITAL ASSETS AND DEBT ADMINISTRATION

a) Capital Assets

The Municipality has invested \$31,861,866 in capital assets used in governmental activities, which have an accumulated depreciation and amortization of \$8,873,792 at June 30, 2012. The net capital assets of governmental activities decreased during the current fiscal year due to the current fiscal year's capital additions (\$303,954), which were totally offset by the depreciation and amortization expense (\$949,129), and capital assets disposal (\$27,758) for the same period.

b) Debt Administration

The Municipality finances a significant portion of its construction activities through bond and notes issuances, and through state and federal grants. 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.

At June 30, 2012, the Municipality's total bonded debt amounted to \$23,272,500, consisting of bonds payable. Such debt is backed by the full faith and credit of the Municipality. The following is a summary of the debt activity for the fiscal year ended June 30, 2012:

- Bonds payable decreased by \$597,000 by the effect of total principal payments on bonds made during the current fiscal year.
- The Municipality has also certain outstanding notes payable due to Puerto Rico Treasury Department (\$288,231). During the year, notes payable to the Treasury Department decreased by \$192,155, the total principal payments on notes made during the current fiscal year.
- The Municipality has also certain outstanding notes payable due to CRIM (\$893,922). Such notes payable decreased by \$70,728 during the current fiscal year due to the principal payments made during the same period.
- Furthermore, the Municipality has estimated the landfill closure and post closure care costs in approximately \$3,260,000.

REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of the Municipality's finances for all of the Municipality's citizens, taxpayers, customers, investors and creditors. This financial report seeks to demonstrate the Municipality's accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Municipality of Santa Isabel, Department of Finance.

Commonwealth of Puerto Rico
Municipality of Santa Isabel
Statement of Net Assets
June 30, 2012

Assets

Current assets:

Cash in commercial banks	\$ 1,054,285
Cash with fiscal agent	6,892,658
Accounts receivable, net of allowance for doubtful accounts:	
Property taxes	26,452
Intergovernmental	1,103,107
Sales tax	207,074
Interest	4,481
Miscellaneous	52,582
Total current assets	9,340,639

Noncurrent assets:

Capital assets, net of accumulated depreciation and amortization of \$8,873,792	22,988,074
Total noncurrent assets	22,988,074
Total assets	\$ 32,328,713

Current Liabilities (due within one year):

Accounts payable	\$ 2,806,456
Intergovernmental payables	917,523
Accrued interest payable on long-term debt	485,482
Deferred revenues	1,235,357
Current portion of long-term obligations:	
Bonds payable	595,000
Other debts	2,581,064
Total current liabilities	8,620,882

Noncurrent liabilities (due in more than one year):

Total liabilities	\$ 34,942,623
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Net assets (liabilities):

Invested in capital assets, net of related debt	\$ 17,680,009
Restricted for:	
Debt service	4,356,602
Other specified purposes	1,369,775
Unrestricted net assets (liabilities)	(26,020,296)
Total net assets (liabilities)	\$ (2,613,910)

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

Commonwealth of Puerto Rico
Municipality of Santa Isabel
Statement of Activities
June 30, 2012

Functions/programs	Expenses	Charges for services	Program Revenues		Net Expenses and Charges in Net Assets
			Operating grants and contributions	Capital grants and contributions	
Governmental activities :					
General government	\$ 6,268,742	\$ -	\$ -	\$ -	\$ (6,268,742)
Urban and economic development	9,913,526	13,528	146,669	2,373,726	(7,379,603)
Public safety	715,630	90,664	-	-	(624,966)
Health and sanitation	922,443	569,988	-	-	(352,455)
Culture, recreation and education	1,599,189	-	655,455	-	(943,734)
Welfare and housing assistance	961,315	-	531,262	-	(430,053)
Interest on long-term obligation	903,213	-	-	-	(903,213)
Total governmental activities	<u>\$ 21,284,058</u>	<u>\$ 674,180</u>	<u>\$ 1,333,386</u>	<u>\$ 2,373,726</u>	<u>\$ (16,902,766)</u>
General Revenues:					
Taxes:					
Property taxes					4,178,828
Municipal license taxes					1,610,585
Sales taxes					748,521
Construction excise taxes					2,256,482
Total taxes					<u>8,794,416</u>
Grants and contributions, not restricted to specific programs					4,810,200
Interests on deposits					103,102
Miscellaneous					224,355
Total general revenues					<u>13,932,073</u>
					Net changes in net assets (liabilities) (2,970,693)
					Net assets at beginning of the year 356,783
					<u>\$ (2,613,910)</u>

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
 Balance Sheet
 Governmental Funds
 June 30, 2012

	MAJOR FUNDS					Total Governmental Funds
	General Fund	State Legislative Joint Resolutions	Capital Improvement Bonds Fund	Debt Service	Other Nonmajor Fund	
ASSETS						
Cash in commercial banks	\$ 359,560	\$ 334,605	\$ -	\$ -	\$ 360,120	\$ 1,054,285
Cash in fiscal agent	221,014	-	1,804,441	4,738,674	128,529	6,892,658
Account receivable, net of doubtful accounts:						
Property taxes	-	-	-	26,452	-	26,452
Sales tax	130,116	-	-	76,958	-	207,074
Interest	4,481	-	-	-	-	4,481
Other	25,000	-	-	-	27,582	52,582
Due from other funds	204,045	1,054,695	-	-	30,479	1,289,219
Due from governmental entities	560,916	-	-	-	542,191	1,103,107
Total assets	\$ 1,505,132	\$ 1,389,300	\$ 1,804,441	\$ 4,842,084	\$ 1,088,901	\$ 10,629,858
LIABILITIES						
Accounts payable	1,785,225	207,507	295,006	-	518,718	2,806,456
Intergovernmental	917,523	-	-	-	-	917,523
Due to other funds	1,084,769	-	-	-	204,450	1,289,219
Deferred revenue	1,618,522	-	-	-	177,751	1,796,273
Matured bonds due and payable	-	-	-	555,000	-	555,000
Matured interests due and payable	-	-	-	485,482	-	485,482
Total liabilities	5,406,039	207,507	295,006	1,040,482	900,919	7,849,953
FUND BALANCE						
Fund Balance:						
Restricted	111,746	1,181,793	1,509,435	3,801,602	187,982	5,610,765
Unassigned	(4,012,653)	-	-	-	-	(4,012,653)
Total fund balances	(3,900,907)	1,181,793	1,509,435	3,801,602	187,982	2,779,905
TOTAL LIABILITIES AND FUND BALANCE	\$ 1,505,132	\$ 1,389,300	\$ 1,804,441	\$ 4,842,084	\$ 1,088,901	\$ 10,629,858

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
 Reconciliation of the Balance Sheet - Governmental Funds
 to the Statement of Net Assets
 June 30, 2012

Aggregate fund balance reported in the balance sheet - governmental funds	\$ 2,779,905
Governmental activities' amounts reported in the statement of net assets and the balance sheet - governmental funds are different because:	
Capital assets used in governmental activities are not financial resources, therefore, are not reported in the governmental funds	22,988,074
Deferred (unavailable) revenues in the governmental funds that are recorded as revenues in the statement of activities	560,916
The following liabilities are not due (mature) in the current period, therefore, are not reported in the governmental funds:	
Accrued employees' christmas bonus	(265,969)
Compensated absences	(1,517,183)
Bonds and notes payable	(22,717,500)
Debt to intergovernmental agencies	(1,182,153)
Landfill closure and postclosure care costs	<u>(3,260,000)</u>
Net assets as reported in the accompanying statement of net assets	<u>\$ (2,613,910)</u>

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Statement of Revenues, Expenditures and
Changes in Fund Balance - Governmental Funds
Year Ended June 30, 2012

	MAJOR FUNDS					Total Governmental Funds
	General Fund	State Legislative Joint Resolutions	Capital Improvement Bonds Fund	Debt Service	Other Non-major Funds	
REVENUES						
Taxes:						
Property taxes	\$ 2,245,028	\$ -	\$ -	\$ 1,776,816	\$ -	\$ 4,021,844
Municipal license	1,610,585	-	-	-	-	1,610,585
Construction excise taxes	748,521	-	-	-	-	748,521
Sales tax	1,469,046	-	-	787,436	-	2,256,482
Charges of service	66,927	-	-	-	593,256	660,183
Intergovernmental grants and contributions:						
Federal government	-	-	-	-	2,863,929	2,863,929
State government	4,796,824	625,807	-	-	185,689	5,608,320
Investment earnings	101,848	-	-	1,252	2	103,102
Miscellaneous	192,655	15	-	-	45,682	238,352
Total Revenues	\$ 11,231,434	\$ 625,822	\$ -	\$ 2,565,504	\$ 3,688,558	\$ 18,111,318
EXPENDITURES						
Current:						
General government	6,091,041	-	-	-	-	6,091,041
Urban and economic development	6,245,883	644,874	1,068,569	-	1,786,821	9,746,147
Public safety	518,517	-	-	-	117,613	636,130
Health and Sanitation	547,435	-	-	-	530,258	1,077,693
Culture, recreation and education	707,609	-	-	-	680,573	1,388,182
Welfare and housing assistance	470,978	-	-	-	482,812	953,790
Debt service:						
Principal	-	-	-	613,000	-	613,000
Interest	-	-	-	903,213	-	903,213
Total Expenditures	14,581,463	644,874	1,068,569	1,516,213	3,598,077	21,409,196
Excess (Deficiency) of Revenues over expenditures	(3,350,029)	(19,052)	(1,068,569)	1,049,291	90,481	(3,297,878)
OTHER FINANCING SOURCES (USES)						
Transfer in from other funds	-	-	-	181,987	-	181,987
Transfer out to other funds	(181,987)	-	-	-	-	(181,987)
Total Other Financing Sources (uses)	(181,987)	-	-	181,987	-	-
NET CHANGE IN FUND BALANCES (DEFICITS)	(3,532,016)	(19,052)	(1,068,569)	1,231,278	90,481	(3,297,878)
FUND BALANCE (DEFICIT) AT BEGINNING OF YEAR	(368,891)	1,200,845	2,578,004	2,570,324	97,501	6,077,783
FUND BALANCE AT END OF YEAR	\$ (3,900,907)	\$ 1,181,793	\$ 1,509,435	\$ 3,801,602	\$ 187,982	\$ 2,779,905

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

Handwritten signature and date:
16/07/2012

Commonwealth of Puerto Rico
Municipality of Santa Isabel
 Reconciliation of Statement of Revenues, Expenditures and Changes
 in Fund Balance - Governmental Funds to the Statements of Activities
 For the Year Ended June 30, 2012

Net change in fund balances- total governmental funds \$ (3,297,878)

Governmental activities amounts reported in the statement of activities and the statement of Revenues, expenditures and changes in fund balances governmental funds are different because:

Revenues in the statement of activities that not provide current financial resources, therefore are not reported as revenues in the funds:

Net Change in CRIM Final Settlement Deferred in GFFS	156,984
Net Change in State Treasury Department Christmas Bonus Reimbursement Deferred in GFFS	45,063

Under the modified accrual basis of accounting used in the governmental funds, expenditures are not recognize for transactions that are not normally paid with expendable financial resources. In the Statements of Activities , however, wich is presented in the accrual basis, expenses and liabilities are presented regardless of when financial resources are available:

Net Change in Compensated Absences Liability	(153,548)
Net Change in Christmas Bonus	(97,022)
Net Change in Landfill Closure and Post closure care costs	160,000
Other intergubernamental debts	247,883

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 as depreciation and amortization expenses. This the amount by which depreciation expenses exceed capital outlays. (645,175)

Repayment of principal of long-term obligation is an expenditures in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets 613,000

Net changes in net assets reported in the accompanying statements of activities \$ (2,970,693)

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

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Basic Financial Statements
June 30, 2012

1. Summary of Significant Accounting Policies

The Municipality of Santa Isabel, Commonwealth of Puerto Rico (the Municipality), is a local municipal government constituted in 1841 in the Commonwealth of Puerto Rico. The Municipality has full legislative, fiscal and all other governmental powers and responsibilities expressly assigned by Law No. 81 of August 30, 1991, as amended, known as *Autonomous Municipalities Act of the Commonwealth of Puerto Rico* (Act No. 81). The Municipality is one of seventy-eight municipal governments legally separated from the state government of the Commonwealth of Puerto Rico (the Commonwealth).

The Constitution of the Commonwealth provides for the separation of powers of the executive, legislative and judicial branches of the Commonwealth and the municipalities. However, the Municipality's governmental system consists of executive and legislative branches only. A Mayor, elected every four years by the citizens, exercises the executive power of the Municipality. The legislative power of the Municipality is exercised by the Municipal Legislature, whose members are also elected every four years. The judiciary power is exercised by the General Justice Court System of the Commonwealth, which has jurisdiction over the Municipality.

The Municipality assumes either partial or full responsibility for providing services to its citizens related to public housing, welfare, public safety, health, sanitation, education, culture, recreation, urban development, economic development, and many other fiscal, general and administrative services.

a) Financial Reporting Model

The accompanying basic financial statements present the financial position of the governmental activities, each major governmental funds, and the aggregate remaining fund information of the Municipality at June 30, 2012, in conformity with Accounting Principles Generally Accepted in the United States of America (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB). In addition, the accompanying basic financial statements present the changes in the financial position (results of operations) of the governmental activities, each major governmental fund, and the aggregate remaining fund information for the fiscal year ended June 30, 2012 in conformity with GAAP.

According to the financial reporting model established by GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB No. 34), the required basic financial statement presentation applicable to the Municipality is composed of the following elements: (1) government-wide financial statements (GWFS), (2) governmental fund financial statements (FFS), (3) notes to basic financial statements, and (4) required supplementary information (RSI).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Basic Financial Statements
June 30, 2012

RSI consists of: (1) a Management's Discussion and Analysis (MD&A) and (2) a budgetary comparison schedule – general fund. *RSI* is unaudited supplementary information required by GAAP presented along with, but separate from, the Municipality's basic financial statements. *MD&A* is a narrative report that introduces the accompanying basic financial statements and provides an analytical overview of the Municipality's financial activities for the fiscal year ended June 30, 2012, based on the Municipality's knowledge of the transactions, events and conditions reflected in the basic financial statements. The MD&A also highlights certain key fiscal policies that control the Municipality's operations.

In addition to the required financial reporting requirements referred to above, the accompanying basic financial statements are accompanied by additional supplementary information consisting of a budgetary comparison schedule – general fund and the notes to the budgetary comparison schedule – general fund, which have been subjected to the auditing procedures applied in the audit of the accompanying basic financial statements as of and for the fiscal year ended June 30, 2012.

b) *Financial Reporting Entity*

The accompanying basic financial statements include all departments, agencies and municipal entities that: (1) are under the legal and administrative control of the Mayor and (2) whose funds are under the legal custody and control of the Municipality's Director of Finance and Budget, as prescribed by Law No. 81.

The Municipality's management has considered all potential component units for which it may be financially accountable and other legally separate organizations for which the nature and significance of their relationship with the Municipality may be such that exclusion of their basic financial statements from those of the Municipality would cause the Municipality's basic financial statements to be misleading or incomplete.

The Municipality's management has concluded that, based on the criteria set forth by GASB Statement No. 14 - *The Financial Reporting Entity* (GASB No. 14) and GASB Statement No. 39- *Determining Whether Certain Organizations are Component Units* (GASB No. 39), there are no legally separate entities or organizations that should be reported as component units of the Municipality as of June 30, 2012 nor for the year then ended.

c) *Government-Wide Financial Statements*

The accompanying GWFS are composed of: (1) the statement of net assets and (2) the statement of activities. These financial statements do not report fund information but rather report information of all of the Municipality's governmental activities. These statements are aimed at presenting a broad overview of the Municipality's finances through reporting its

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Basic Financial Statements
June 30, 2012

financial position and results of operations as a whole, using methods that are similar to those used by most private businesses.

The focus of the GWFS is not on compliance with budgets, regulatory requirements or on the use of available or currently expendable financial resources (referred to as fiscal accountability), but on operational accountability information about the Municipality as a single economic unit. Operational accountability is the Municipality's responsibility to report to the extent to which it has met its operating objectives efficiently and effectively, using all resources available for that purpose. It focuses on the Municipality's principal operating objective, which is to provide services to its citizens.

The accompanying statement of net assets provides short-term and long-term information about the Municipality's financial position and condition by presenting all of the Municipality's assets and liabilities, with the difference between these two items reported as "net assets" (equity). This statement assists management in assessing the level of services that can be provided by the Municipality in the future, and its ability to meet its obligations as they become due. In addition, this statement reports the extent to which the Municipality has invested in capital assets, including infrastructure, and discloses legal and contractual restrictions on resources.

Net assets are classified in the accompanying statement of net assets within the following three categories:

- **Invested in capital assets, net of related debt** – These consist of capital assets, net of accumulated depreciation and amortization, reduced by the outstanding balances of bonds, notes and other debt that are attributed to the acquisition, construction or improvement of those assets. For the purposes of determining the outstanding debt attributed to capital assets, the total long-term debt related to the acquisition, construction or improvement of capital assets have been reduced by any related unspent debt proceeds and any related unamortized debt issuance costs.
- **Restricted net assets** – These consist of net assets restricted by external parties (such as creditors, grantors, contributors, laws or regulations of other governments, etc.), or net assets for which constraints are imposed by constitutional provisions or enabling legislation. Enabling legislation is defined as legislation that authorizes the Municipality to assess, levy, charge or otherwise mandate payment of resources (from external resource providers). Enabling legislation establishes restrictions if it includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation.

The classification of restricted net assets identifies resources that have been received or earned by the Municipality with an explicit understanding between the Municipality

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and the resource providers that the resources would be used for specific purposes. Grants, contributions and donations are often given under those kinds of conditions. Bond indentures also often limit the use of bond proceeds to specific purposes.

Internally imposed designations of resources, including earmarking, are not reported as restricted net assets. These designations consist of management's plans for the use of resources, which are subject to change at the discretion of the Municipal Legislature.

- **Unrestricted net assets** – These consist of net assets that are neither externally or legally restricted, nor invested in capital assets. However, unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints that are imposed by management, but can be removed or modified.

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

The accompanying statement of activities presents the Municipality's results of operations by showing, how the Municipality's net assets or liabilities changed during the fiscal year ended June 30, 2012, using a net (expense) revenue format. This statement presents the cost of each function/program as well as the extent to which each of the Municipality's functions, programs or other services either contributes to or draws from the Municipality's general revenues (such as property taxes, municipal license taxes, construction excise taxes, etc.).

A function/program describes a group of activities that are aimed at accomplishing a major service or regulatory responsibility. The functions/programs reported in the accompanying basic financial statements are: (1) general government, (2) urban and economic development, (3) public safety, (4) health and sanitation, (5) culture, recreation and education, and (6) welfare and housing assistance. The governmental operations of the Municipality's departments and operational units are classified within the following functions/programs in the accompanying basic financial statements:

General Government:

Municipal Legislature
Mayor's Office
Department of Finance
Department of Human Resources
Department of Municipal Secretary
Department of Internal Audit

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Urban and Economic Development:

Department of Public Works

Public Safety:

Department of Municipal Police

Office of Emergency Management

Health and Sanitation:

Department of Health

Culture, Recreation and Education:

Department of Recreation and Sports

Welfare and Housing Assistance:

Department of Elderly Affairs

Department of Service to Citizen

The statement of activities demonstrates the degree to which program revenues offset direct expenses of a given function/program or segments. Direct expenses are those that are clearly identifiable with a specific function, segment or operational unit. This statement reports revenues in three broad categories: (1) program revenues, (2) general revenues and (3) special items.

Program revenues are generated directly from a program itself or may come from parties outside the Municipality's taxpayers or citizens. In the statement of activities, program revenues reduce the costs (expenses) of the function/program to arrive at: (1) the net cost of the function/program that must be financed from the Municipality's general revenues or (2) the net program revenue that contributes to the Municipality's general revenues. The accompanying statement of activities separately reports the following categories of program revenues:

- **Charges for services** – These revenues generally consist of exchange or exchange-like transactions involving charges to customers or applicants who purchase, use or directly benefit from the goods, services or privileges provided, or are otherwise directly affected by the services. These revenues include fees charged for specific services, rent, charges for licenses and permits, and fines and forfeitures, among others.
- **Program-specific operating and capital grants and contributions** – These revenues consist of transactions that are either mandatory or voluntary non-exchange transactions with other governments, organizations, or individuals that restrict the resources for use in a particular program. Operating grants and contributions consist of resources that are required to be used to finance the costs of operating a specific program or can be used either for operating or capital purposes of a specific program. Capital grants and contributions consist

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of revenues or resources that are restricted for capital purposes – to purchase, construct or renovate capital assets associated with a specific program. Restricted operating and capital grants and contributions are program revenues because they are specifically attributable to a program and reduce the net expense of that program to the Municipality. They are reported net of estimated uncollectible amounts.

General revenues are the default category for revenues. It includes all revenues and gains that do not meet the definition of program revenues. Property taxes, municipal license taxes, construction excise taxes and sales and use taxes are reported as general revenues. All other nontax revenues (including unrestricted interest on deposits, grants and contributions not restricted for specific programs and miscellaneous revenues) that do not meet the definition of program revenues are classified as general revenues. Resources that are dedicated internally by the Municipality are reported as general revenues rather than as program revenues. All general revenues are reported net of estimated uncollectible amounts, which are recorded as reduction of revenues rather than as expenses.

The general government function/program reported in the accompanying statement of activities includes expenses that are, in essence, indirect or costs of other functions/programs of the Municipality. Even though some of these costs have been charged to certain funds in the FFS as indirect cost allocations permitted under some federal programs, the Municipality has reported these indirect costs as direct expenses of the general government function. Accordingly, the Municipality generally does not allocate general government (indirect) costs to other functions.

The effects of all inter-fund governmental activities (revenues, expenditures and other financing sources/uses among governmental funds) have been removed from the accompanying statements of net assets and activities.

The Municipality classifies the most significant portion of its activities as governmental activities in the accompanying GWFS. These are activities generally financed through taxes, intergovernmental revenues and other non-exchange revenues that can be used to support the Municipality's programs or services. These governmental activities are also generally reported in the FFS.

The Municipality has no fiduciary activities, which are those in which the Municipality would be holding or managing net assets for specific individuals or other external parties in accordance with trust agreements or other custodial arrangements. In addition, the Municipality has no operations or activities that are primarily financed and operated in a manner similar to private business enterprises, where the costs of providing goods or services to the general public is financed primarily through user charges.

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d) Governmental Fund Financial Statements

The accompanying GFFS are composed of: (1) the balance sheet – governmental funds and (2) the statement of revenues, expenditures and changes in fund balances – governmental funds. These financial statements report the financial position and results operations of the Municipality's governmental funds by presenting sources, uses and balances of current financial resources. Some of these financial statements have a budgetary orientation and focus primarily on: (1) the Municipality's major funds, as defined below, (2) the fiscal accountability and (3) the individual parts of the Municipality's government. Fiscal accountability represents the Municipality's responsibility to justify that its actions in the current year have complied with public decisions concerning the raising and spending of public moneys in the short term (one fiscal year).

Each governmental fund is considered an independent fiscal entity accounted for within a set of self-balancing accounts that comprise its assets, liabilities, fund equity or deficit, revenue and expenditures. The accompanying GFFS segregate governmental funds according to their intended purpose and are used in demonstrating compliance with legal, financial and contractual provisions. The minimum number of governmental funds is maintained consistent with legal and self-imposed managerial requirements established by the Municipality. For financial reporting purposes, the Municipality classifies its governmental funds within the following categories:

- **General fund** – The general fund is the Municipality's main operating fund and a major governmental fund, as defined below, used to account for all financial resources and governmental activities not accounted for and reported in another fund. It is presumed that the Municipality's governmental activities have been reported in the general fund except for transactions for which one of the following compelling reasons has required the use of another fund: (1) legal requirements, (2) GAAP requirements or (3) the demands of sound financial administration requiring the use of a governmental fund other than the general fund.
- **Special revenue funds** – The special revenue funds are major and non-major governmental funds, as defined below, used by the Municipality to account for the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service and capital projects. The uses and limitations of each special revenue fund are specified by municipal ordinances or federal and state statutes. However, resources restricted to expenditure for purposes normally financed from the general fund are reported in the Municipality's general fund provided that all applicable legal requirements are appropriately satisfied. In this case, a special revenue fund to account for such kind of transactions will be used only if legally mandated.
- **Debt service fund** – The debt service fund is a major governmental fund, as defined below, used by the Municipality to account for all financial resources that are restricted, committed, or assigned to expenditure for principal and interest; for (1) bonds payable for which debt

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service payments are legally mandated to be accounted for in a debt service fund and/or (2) bonds payable or any general long-term debt for which the Municipality is being accumulating financial resources in advance to pay principal and interest payments maturing in future years. During the fiscal year ended June 30, 2012, the financial activity accounted for in the debt service fund was specifically related to bonds payable.

The outstanding balance of general long-term obligations for which debt service payments do not involve the advance accumulation of resources (such as notes payable, obligations under capital leases, accrued compensated absences, and claims and judgments) are only accounted for in the accompanying statement of net assets. The debt service payments of such debts, as applicable, are generally accounted for in the general fund.

- **Capital projects funds** – Capital projects funds are major and non-major governmental funds, as defined below, used to account for all financial resources that are restricted, committed, or assigned to expenditure for capital outlays. Significant capital outlays financed from proceeds of general obligation, public improvement or special obligation bonds are accounted for also in the capital projects funds.

The use of the capital projects funds has been reserved only for major capital acquisitions, construction or improvement activities that would distort financial resources trend data if not reported separately from the other Municipality's operating activities. The routine purchases of minor capitalizable assets (such as furniture, office equipment, vehicles and other minor capital assets or improvements) have been reported in the governmental fund from which financial resources were used for the payment.

The focus of the FFS is on major governmental funds and fund types, which generally represent the Municipality's most important funds. Accordingly, the Municipality is required to segregate governmental funds and fund types between major and non-major categories within the FFS. Major individual governmental and proprietary funds and fund types are reported individually as separate columns in the FFS, while data from all non-major governmental funds are aggregated into a single column, regardless of fund type.

By definition, the Municipality's general fund is always considered a major governmental fund for financial reporting purposes. In addition, any other governmental fund is classified as a major governmental fund in the FFS if its total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding element total (assets, liabilities, revenues or expenditures) for all governmental funds. In addition, the same element that meets the 10 percent criterion must be at least 5 percent of the corresponding element total for all governmental and enterprise (proprietary) funds combined. For the purposes of applying the aforementioned major fund criteria, no eliminations of inter-fund balances have been made. Total revenues for these purposes means all revenues, including operating and non-operating revenues (net of allowances for uncollectible accounts), except for other financing sources. Total

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expenditures\expenses for these purposes mean all expenditures\expenses, including operating and non-operating expenditures\expenses, except for other financing uses.

Based on the aforementioned criteria, the Municipality's major governmental funds reported in the accompanying governmental fund financial statements are: (1) the general fund, (2) the capital improvement bond fund, (3) the legislative joint resolutions fund, and (3) debt service fund.

The Capital Improvement Bond Fund is a major capital projects fund used to account for proceeds of general obligation, public improvement or special obligation bonds. These proceeds are used for the acquisition, construction or improvement of major capital facilities and other assets.

The State Legislative Joint Resolutions Fund is a major fund used to account for financial resources derived from capital and operating grants awarded each year by the Commonwealth's Senate and House of Representatives (the Commonwealth's Legislature). The purpose of the amounts awarded by the Commonwealth's Legislature vary from year to year, but are generally restricted to (1) partially subsidy certain qualifying administrative and operational activities of the Municipality, (2) provide specific multipurpose services to citizens and (3) finance the acquisition or construction of capital assets approved by the Commonwealth's Legislature.

The Debt Service Fund is used to account for the accumulation of recourses for and the payment of, general long-term debt principal, interest, and related cost.

The accompanying FFS are accompanied by other statements and schedules required by GAAP: (1) the reconciliation of the balance sheet – governmental funds to the statement of net assets, and (2) the reconciliation of the statement of revenues, expenditures and changes in fund balances – governmental funds to the statement of activities.

e) Measurement Focus and Basis of Accounting

Government-wide financial statements – The accompanying GWFS are prepared using the economic resources measurement focus and the accrual basis of accounting. Subject to the additional rules and limitations detailed below, revenues (including interest on deposits and rent) are generally recorded when earned and expenses are generally recorded when a liability is incurred, regardless of the timing of related cash flows.

All revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are generally recorded when the exchange takes place. In exchange transactions, each party to the transaction receives and gives up essentially equal values. An exchange-like transaction is one in which there is an identifiable exchange and the values exchanged, though related, may not be quite equal. Nevertheless, the exchange characteristics of the exchange-like

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transaction are strong enough to justify treating it as an exchange for accounting purposes (examples include certain charges for services and miscellaneous revenues, which are recorded as revenues when collected because they are generally not measurable until actually received).

All revenues, expenses, gains, losses and assets resulting from non-exchange transactions are recorded using the criteria set forth by GASB Statement No. 33, *Accounting and Financial Reporting for Non-exchange Transactions* (GASB No. 33). GASB No. 33 established accounting and reporting standards for non-exchange transactions involving cash and financial or capital resources (for example, most taxes, grants and private donations). In a non-exchange transaction, the Municipality gives (or receives) value without directly receiving (or giving) equal value in return. This is different from an exchange transaction, in which each party receives and gives up essentially equal values. According to GASB No. 33, the Municipality groups its non-exchange transactions into the following four classes in the accompanying basic financial statements: (a) derived tax revenues, (b) imposed non-exchange revenues, (c) government mandated non-exchange transactions, and (d) voluntary non-exchange transactions.

In the case of derived tax revenue transactions, which result from assessments the Municipality places on exchange transactions, receivables and revenues are recorded when the underlying exchange has occurred.

In the case of imposed non-exchange revenue transactions (such as property taxes and municipal license taxes), which result from assessments made by the Municipality on nongovernmental entities, including individuals, other than assessments on exchange transactions, receivables are generally recorded in the period when an enforceable legal claim has arisen. Property taxes and municipal license are generally recorded as revenues (net of amounts considered not collectible) in the fiscal year when resources are required to be used or the first fiscal year that the use of the resources is permitted.

Government-mandated non-exchange transactions (such as grants and contributions) result when a government at one level (such as the federal or state government) provides resources to another government (such as the Municipality), and the provider government requires the recipient government to use those resources for a specific purpose or purposes established in the provider's enabling legislation. In these types of transactions, receivables and revenues are generally recorded as follows:

- For reimbursement-type (commonly known as "expenditure-driven awards"), receivables and revenues are recorded when all eligibility requirements imposed by the provider have been met. The Municipality must expend resources on the specific purpose or project before the provider reimburses any amounts. Revenue is, therefore, generally recognized as qualifying reimbursable expenditures are incurred.

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- For other types of grants (mainly grants and contributions with purpose restrictions but with no time requirements), receivables and revenues are recorded when all applicable eligibility requirements are met. When the provider is a government (including the government of the United States of America) the applicable recognition period for both, the provider and the recipient, is the provider's fiscal year and begins on the first day of that year.

Voluntary non-exchange transactions (such as donations and certain grants and entitlements) result from legislative or contractual agreements, other than exchanges, willingly entered into by two or more parties. In these types of transactions, receivables and revenues are generally accounted for in the same manner as government-mandated non-exchange transactions discussed above. Events that are neither exchange nor non-exchange transactions are recorded when it is probable that a loss has been incurred and the amount of loss is reasonably estimable.

Receipts of any type of revenue sources collected in advance for use in the following fiscal year are recorded as unearned revenues.

According to GASB No. 34, all general capital assets and the unmatured long-term liabilities are recorded only in the accompanying statement of net assets. The measurement focus and the basis of accounting used in the accompanying GWFS differ significantly from the measurement focus and basis of accounting used in the preparation of the accompanying governmental fund financial statements. Therefore, the accompanying governmental fund financial statements include reconciliations, as detailed in the accompanying table of contents, to better identify the relationship between the GWFS and the governmental fund financial statements.

Governmental fund financial statements – The accompanying governmental fund financial statements are reported using the current financial resources measurement focus (flow of current financial resources) and the modified accrual basis of accounting. Accordingly, the accompanying statement of revenues, expenditures and changes in fund balances (deficits) – governmental funds, reports changes in the amount of financial resources available in the near future as a result of transactions and events of the fiscal year reported. Therefore, revenues are generally recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current fiscal year or soon enough thereafter to pay liabilities of the current fiscal year. For this purpose, the Municipality considers most revenues to be available if collected generally within 90 days after June 30, 2012, except for property taxes for which the availability period is 60 days. Revenue sources not meeting this availability criterion or collected in advance are recorded as deferred (earned and unavailable) revenues at June 30, 2012.

The principal revenue sources considered susceptible to accrual include property taxes, municipal license taxes, sales and use taxes, construction excise taxes, intergovernmental grants and contributions, interest on deposits and charges for services. These principal revenue sources meet

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both measurability and availability criteria in the accompanying governmental fund financial statements, except for amounts recorded as deferred (earned and unavailable) revenues.

In a manner similar to the GWFS, but subject to and limited by the availability criteria discussed previously, all revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are also generally recorded when the exchange takes place. Accordingly, certain charges for services and miscellaneous revenues are recorded as revenues when collected because they are generally not measurable until actually received.

All revenues, expenses, gains, losses and assets resulting from non-exchange transactions are recorded in a similar manner to the GWFS, using the previously discussed criteria set forth by GASB No. 33 for non-exchange transactions, but subject to and limited by the availability criteria discussed above. Accordingly, property tax and municipal license tax receivables are also generally recorded in the fiscal year when an enforceable legal claim has arisen while property tax and municipal license tax revenues (net of amounts considered not collectible) are also generally recorded in the fiscal year when resources are required to be used or the first fiscal year that the use of the resources is permitted. Receivables and revenues from federal and state grants and contributions, donations and entitlements are also generally recorded when all eligibility requirements imposed by the provider have been met (generally, as qualifying reimbursable expenditures are incurred for expenditure-driven grants).

Interest on deposits is recorded when earned only if collected within 90 days after the fiscal year-end since these revenues would be considered both measurable and available.

Pursuant to the provisions of GASB Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements* (GASBI No. 6), in the absence of an explicit requirement (i.e., the absence of an applicable modification, discussed below) the Municipality generally accrues a governmental fund liability and an expenditure (including salaries, professional services, supplies, utilities, etc.) in the period in which the government incurs the liability, to the extent that these liabilities are normally expected to be liquidated with current available financial resources. GASBI No. 6 modified the recognition criteria for certain expenditures and liabilities reported under the modified accrual basis of accounting prior to GASB No. 34, and clarified a number of situations in which the Municipality should distinguish between governmental fund liabilities and general long-term liabilities. Therefore, the accompanying balance sheet – governmental funds generally reflects assets that will be converted into cash to satisfy current liabilities. Long-term assets (except for accounts receivables and inter-fund advances) and those assets that will not be converted into cash to satisfy current liabilities are generally not accounted for in the accompanying balance sheet – governmental funds. At the same time, long-term liabilities (generally, those unmatured that will not require the use of current financial resources to pay them) are not accounted for in the accompanying balance sheet – governmental funds.

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Modifications to the accrual basis of accounting in accordance with GASBI No. 6 include:

- Principal and interest on bonds payable are recorded when they mature (when payment is due), except for principal and interest due on July 1, 2012, which have been recorded as governmental fund liabilities at June 30, 2012, which is the date when resources are available in the debt service fund (generally, June 30).
- Notes payable, obligations under capital leases, compensated absences, and amounts subject to accrued claims and judgments under litigation are recorded only when they mature (when payment is due).
- Certain accrued liabilities not due and payable or not normally expected to be liquidated with current available and expendable financial resources are recorded in the accompanying statement of net assets. Such liabilities are recorded in the governmental funds when they mature.
- Executory purchase orders and contracts are recorded as assignments of fund balance in the governmental funds FFS.

Liabilities outside the bounds of these exceptions or modifications are reported as governmental fund liabilities when incurred (including salaries, professional services, supplies, utilities, etc.) since these liabilities normally are paid in a timely manner and in full from current financial resources.

The measurement focus of the GFFS is on decreases in net financial resources (expenditures) rather than expenses. Most expenditures are measurable and are recorded when the related governmental fund liability is incurred. Allocation of costs, such as depreciation and amortization, are recorded in the accompanying statement of activities, but are not recorded in the accompanying GFFS.

Under the financial reporting model established by GASB No. 34, all general capital assets and the unmatured long-term liabilities (determined using the modified accrual basis of accounting) are no longer reported in account groups within the governmental fund balance sheet but are incorporated into the accompanying statement of net assets since July 1, 2003.

f) Stewardship, Compliance and Accountability

Budgetary Control

According to Law No. 81, the Mayor and its Administrative Cabinet prepare annual budgets each fiscal year for the Municipality's general fund and debt service fund. Such legally adopted budgets are based on expected expenditures by program and estimated resources by source. The

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annual budgets are developed using elements of performance-based program budgeting and zero-based budgeting, and include estimates of revenues and other resources for the ensuing fiscal year under laws and regulations existing at the time the budgets are prepared.

The Mayor must submit, for each fiscal year commencing on July 1, an annual budgetary resolution project (the Project) to the Commissioner of Municipal Affairs of the Commonwealth (the Commissioner) and the Municipal Legislature no later than the immediately preceding May 31. The Commissioner preliminarily verifies that the Project complies with all the applicable laws and regulations and may provide comments and suggestions to the Mayor on or before the immediately preceding June 15.

The Municipal Legislature has 10 business days, up to the immediately preceding June 13, to discuss and approve the Project with modifications. The Municipal Legislature may amend the budgets submitted by the Mayor but may not increase any items so far to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. After the Municipal Legislature modifies and preliminarily approves the Project, the modified Project is sent back to the Mayor for his approval or rejection within six (6) days. The Mayor may decrease or eliminate any line item but may not increase or insert any new line item in the budgets. The Mayor may also veto the budgets in their entirety and return it to the Municipal Legislature with his objections. If the Mayor rejects the Project, the Municipal Legislature will have up to eight (8) days to adopt or reject the recommendations or objections of the Mayor. The approved Project is sent again to the Mayor, which then would have three (3) days to sign and approve it.

If the budgets are not adopted prior to the end of the deadlines referred to above, the annual budgets for the preceding fiscal year, as approved by the Legislature and the Mayor, are automatically renewed for the ensuing fiscal year until the Municipal Legislature and the Mayor approve new budgets. This regulation permits the Municipality to continue doing payments for its operations and other purposes until the new budgets are approved.

The annual budgets may be updated for any estimate revisions as well as fiscal year-end encumbrances, and may include any additional information requested by the Municipal Legislature. The Mayor may request subsequent amendments to the approved budgets, which are subject to the approval of the Municipal Legislature.

The Municipality's Department of Finance has the responsibility to ensure that budgetary spending control is maintained. For day-to-day management control purposes, expenditures plus encumbrances may not exceed budgeted amounts at the expenditure-type level of each cost center (activity within a program within a fund). The Mayor may transfer unencumbered appropriations within programs within funds. The Municipal Legislature may transfer amounts among programs within and among funds.

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The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriation) is at the function/program level (general government, urban and economic development, public safety, health and sanitation, culture, recreation and education, and public housing and welfare) within a fund.

Under the laws and regulations of the Commonwealth, the appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided.

Budgetary Accounting

The Municipality's annual budgets are prepared using the budgetary (statutory) basis of accounting, which is not in accordance with GAAP.

According to the budgetary basis of accounting, revenue is generally recorded when cash is received. Short-term and long-term borrowings may be used to finance budgetary excess of expenditures over revenues.

The Municipality uses encumbrance accounting to record the full amount of purchase orders, contracts and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control. Accordingly, expenditures are generally recorded when the related expenditure is incurred or encumbered. Available appropriations and encumbrances are established to lapse one fiscal year after the end of the fiscal year. Amounts required to settle claims and judgments against the Municipality, and certain other liabilities, are not recognized until they are encumbered or otherwise processed for payment. Unencumbered appropriations and encumbrances lapse at fiscal year-end. Other appropriations, mainly capital projects 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 accompanying budgetary comparison schedule – general fund and the budgetary comparison schedule – debt service fund provide information about the general and debt service funds' original budgets, its amendments, and the actual results of operations of such major governmental funds under the budgetary basis of accounting for the fiscal year ended June 30, 2012. Further details of the Municipality's budgetary control at the legal level may be obtained from the Budgetary Liquidation Report for the fiscal year ended June 30, 2012.

Because accounting principles applied for the purposes of the developing data on a budgetary basis differ significantly from those used to present the governmental fund financial statements in conformity with GAAP, a reconciliation of the differences between the general and debt service

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funds' budgetary bases and GAAP actual amounts are presented at the bottom of the respective budgetary comparison schedules.

g) *Unrestricted and Restricted Deposits*

The Municipality's deposits are composed of cash on hand, demand deposits and cash equivalents in: (1) commercial banks, (2) the Government Development Bank for Puerto Rico (GDB), a governmental bank and a major component unit of the Commonwealth, who is statutorily designated as fiscal agent of the Municipality, and (3) the Municipal Revenue Collection Center (CRIM, by its Spanish acronyms), a governmental entity responsible for the imposition and collection of property taxes on behalf of all municipalities of Puerto Rico.

The Municipality follows the practice of pooling cash. The balance in the pooled cash account is available to meet current operating requirements. Under the laws and regulations of the Commonwealth, public funds deposited by the Municipality in commercial banks must be fully collateralized for the amounts deposited in excess of the federal depository insurance generally provided by the Federal Deposits Insurance Corporation (FDIC). All securities pledged as collateral are held by agents designated by the Secretary of the Treasury of the Commonwealth, but not in the Municipality's name.

Restricted assets include cash and cash equivalents in commercial banks, GDB and CRIM. These cash balances are classified as restricted assets since its use is limited for the specified purposes discussed below, which are established by applicable agreements or required by law.

Restricted cash with fiscal agent in the general and debt service funds represent property tax collections which are retained and restricted for the payment of the Municipality's debt service, as established by law. Restricted cash in fiscal agent in other governmental funds consists of unspent proceeds of bonds and notes, and the balance of interest and noninterest bearing accounts which are restricted for: (1) the acquisition, construction or improvement of major capital assets and the operations of federal and state funded programs.

h) *Unrestricted and Restricted Accounts Receivable*

Accounts receivable consist of all revenues earned but not collected at June 30, 2012. These accounts receivables are stated net of estimated reserved for doubtful accounts, which are determined based upon past collection experience, historical trends, current economic conditions and the periodic aging of accounts receivable.

Activities among 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

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funds". Advances between funds, as reported in the GFFS, 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.

i) Capital Assets

Capital assets used in governmental activities include land and land improvements, buildings, structures and building improvements, machinery and equipment (including equipment held under capital leases), furniture and fixtures, licensed vehicles, construction in progress, and infrastructure. These assets are capitalized and reported in the accompanying statement of net assets. Infrastructure assets are generally stationary in nature and include roads, bridges, streets and sidewalks, drainage systems and other similar assets.

For financial reporting purposes, the Municipality defines capital assets as assets with an individual cost basis of \$100 or more at the date of acquisition, construction or improvement, and with useful lives extending beyond one year. All assets with individual costs under \$100 or with useful lives not exceeding one year, are charged directly to expense in the government-wide statement of activities and the statement of revenues, expenses and changes in fund net assets. In the governmental funds, all capital assets are recorded as expenditures in the corresponding function/program identified with the asset.

In the statement of net assets, all capital assets are recorded at cost or estimated historical cost if actual cost was unavailable, except for donated capital assets, which are recorded at their estimated fair value at the date of donation. Estimated historical costs based on deflated current costs were used to value a portion of the infrastructure constructed or acquired prior to June 30, 2003 and certain lands, buildings, structures and building improvements. The method used to deflate the current costs with an approximate price index was used only in the case of certain items for which the historical cost documentation was not available. Actual historical costs were used to value the infrastructure acquired or constructed after June 30, 2003 as well as, construction in progress, machinery and equipment and licensed vehicles acquired prior or after such date.

Major outlays for capital assets and improvements are capitalized in the statement of net assets as projects are constructed. The costs of normal maintenance and repairs that do not add value to the asset or materially extend capital asset lives are not capitalized.

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Depreciation and amortization expense is recorded only in the government-wide statement of activities. However, there is no depreciation or amortization recorded for land and construction in progress. Depreciable capital assets are generally depreciated or amortized over their estimated useful lives under the straight-line method, except for machinery and equipment held under capital leases which is depreciated over the shorter of its estimated useful life or the lease term. The estimated useful lives of major capital asset categories are:

	<u>Years</u>
Land improvements	20
Buildings, structures and building improvements	30 to 50
Infrastructure	20 to 50
Licensed vehicles	8
Furniture and fixtures	5 to 20
Machinery and equipment, excluding those held under capital leases	5 to 20

Depreciation and amortization expense on capital assets are recorded as direct expenses of the function/program specifically identified with the asset. Depreciation and amortization of infrastructure is not allocated to various functions/programs but reported as direct expenses of the urban and economic development function.

j) Deferred Revenues

In the governmental fund financial statements, deferred revenue arises when one of the following situations occur:

- Potential revenue does not meet both the “measurable” and “available” criteria for revenue recognition in the current period (reported as “*earned and unavailable revenue*” in the accompanying balance sheet-governmental funds). As previously discussed, available is defined as due (or past due) at June 30, 2012 and collected within 90 days (60 days for property taxes) thereafter to pay obligations due at June 30. In subsequent periods, when both criteria (measurable and available) are met, the liability for deferred revenue is removed and revenue is recognized.
- The Municipality receives resources before it has a legal claim to them (reported as “*unearned revenue*” in the accompanying balance sheet-governmental funds). In subsequent periods, when the revenue recognition criterion is met, the liability for deferred revenue is removed and revenue is recognized.

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Unearned revenues at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them.

k) Compensated Absences

The liability for compensated absences recorded in the accompanying statement of net assets is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2012 and (2) is not contingent on a specific event that is outside the control of the Municipality and the employee (such as illness). Compensated absences that relate to future services or are contingent on a specific event outside the control of the employer or the employee are accounted for in the period when those services are rendered or those events take place.

The liability for compensated absences includes salary-related costs, which are directly and incrementally related to the amount of salary paid to the employee (such as employer's share of social security taxes and medicare taxes).

The vacation policy of the Municipality provides for the accumulation of regular vacations at a rate of 2.5 days per month (30 days per fiscal year) per employee. Employees accumulate regular sick leave at a rate of 1.5 days per month (18 days per fiscal year). Employees accumulate compensatory time at a rate of 1.5 times the overtime worked. All vacation and sick leave days accumulated by employees in excess of 30 days and 90 days, respectively, are paid to employees each fiscal year, if not consumed, as required by law. In the case of compensatory time, the excess of 240 hours is paid to employees each fiscal year, if not consumed.

Upon termination of employment, an employee receives compensation for all accumulated unpaid regular vacation leave at the current rate. In the case of regular sick leave, if the employee terminates his or her employment before reaching 10 years of services, such regular sick leave is not paid to the employee, if not consumed. In addition upon termination of employment, an employee does not receive compensation for compensatory time, if not consumed previously. After 10 years of services, any regular sick leave balance is paid to the employee. Accumulated vacation time is fully vested to the employee at any time.

The liability for compensated absences is in the statement of net assets. A liability for compensated absences is reported in the governmental fund financial statements only when matured (when payment is due), for example, as a result of employee resignations or retirements.

l) Long-term Debt

The long-term liabilities reported in the accompanying statements of net assets include the Municipality's bonds payable, notes payable, obligations under capital leases, accrued compensated absences and accrued legal claims and judgments.

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All long-term debt to be repaid from governmental resources is reported as liabilities in the accompanying statement of net assets. In the governmental fund financial statements, the face amount of debt issued (gross debt proceeds) is reported as other financing sources when issued.

Non-interest bearing notes payable are accounted for under the provisions of Opinion No. 21, *Interest on Receivables and Payables*, issued by the Accounting Principles Board (APB No. 21). According to APB No. 21, the Municipality has recorded such notes at present value with an imputed interest rate that approximates the rate that would have been used, using the same terms and conditions, if it had been negotiated by an independent lender. In the accompanying statement of net assets, such notes payable are reported net of the applicable unamortized discount, which is the difference between the present value and the face amount of the notes.

m) Accounting for Pension Costs

For the purpose of applying the requirements of GASB Statement No. 27, Accounting for Pensions by State and Local Government Employers (GASB No. 27), the Commonwealth of Puerto Rico is considered to be the sponsor of the Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities (ERS) and System 2000, the two retirement systems in which the employees of the Municipality participate. Accordingly, the Municipality is considered a participant and not a sponsor of these retirement systems since the majority of the participants in the aforementioned pension trust funds are part of the financial reporting entity of the Commonwealth. Accordingly, no portion of the net pension obligation (NPO) related to ERS has been allocated to the Municipality in the accompanying basic financial statements. The basic financial statements of the Commonwealth account for the total amount of the net pension obligation of ERS, including any amount that may be allocated to the Municipality.

According to GASB No. 27, the Municipality accounts for pension costs from the standpoint of a participant in a multiple-employer cost-sharing plan. Accordingly, pension costs recognized in the accompanying basic financial statements are equal to the statutorily required contributions, with a liability recorded for any unpaid required contributions.

n) Risk Management

The Municipality carries commercial insurance covering casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Commonwealth's Department of Treasury (the Department of Treasury) on behalf of all municipalities of Puerto Rico. The Department of Treasury pays the insurance premiums on behalf of the Municipality and then is reimbursed each fiscal year through monthly equal payments deducted from the Municipality's gross property tax collections made by the Municipal Revenue Collection Center ("CRIM", by its Spanish acronym), a governmental entity responsible for billing and collecting property taxes on behalf of all municipalities of Puerto Rico.

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The Municipality carries insurance coverage for death and bodily injuries caused by automobile accidents. This insurance is obtained through the Automobile Accidents Compensation Administration (ACAA, by its Spanish acronym), a component unit of the Commonwealth. This insurance is compulsory for all licensed vehicles used on public roads and highways in Puerto Rico. The annual premium applicable at June 30, 2012 is \$35 per licensed motor vehicle, which is paid directly to ACAA.

The Municipality obtains workers' compensation insurance coverage through the State Insurance Fund Corporation (SIFC), a component unit of the Commonwealth. This insurance covers workers against injuries, disability or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment. Workers' compensation insurance premiums are also paid through monthly deductions made by CRIM from the Municipality's gross property tax collections.

The Municipality obtains unemployment compensation, non-occupational disability, and drivers' insurance coverage for its employees through various insurance programs administered by the Commonwealth's Department of Labor and Human Resources (DOL). These insurance programs cover workers against unemployment and provide supplementary insurance coverage for temporary disability, or death because of work or employment-related accidents or because of illness suffered as a consequence of their employment. Unemployment compensation, non-occupational disability and drivers' insurance premiums are paid directly to DOL on a cost reimbursement basis.

The Municipality also obtains medical insurance coverage from a health insurance company for its employees. Different health insurance coverage and premium options are negotiated each year by the Municipality. The current insurance policies have not been cancelled or terminated at June 30, 2012. Premiums are paid on a monthly basis directly to the insurance company. In the past three years, the Municipality has not settled claims that exceeded insurance coverage.

o) Fund Balances

On July 1, 2010, the Municipality adopted the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions No. 54* (GASB No. 54). GASB No. 54, which enhanced the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied. Also, this statement establishes fund balance classifications that comprise a hierarchy upon use of the resources reported in governmental funds.

Pursuant to the provisions of GASB No. 54, the accompanying GFFS report fund balance amounts that are considered restricted, committed, assigned, and unassigned, based on the relative strength of constraints that control how specific amounts can be spent, as defined below:

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- ***Nonspendable*** – Represent resources that cannot be spent due to form, for example, inventories and prepaid amounts. Also, long-term loan and note receivables, and property held for resale would be reported here unless the proceeds are restricted, committed or assigned. Amounts that must be maintained intact legally or contractually (corpus or principal of a permanent fund).
- ***Restricted*** – Represent resources that can be spent only for the specific purposes stipulated by constitutional provisions, external resource providers (externally imposed by creditor or grantors), or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use). Effectively, restrictions may be changed or lifted only with the consent of resource providers.
- ***Committed*** – Represent resources used for specific purposes, imposed by formal action of the Municipality's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.
- ***Assigned*** – Represent resources intended to be used by the Municipality for specific purposes but do not meet the criteria to be classified as restricted or committed (generally executive orders approved by the Mayor). Intent can be expressed by the Municipal Legislature, the Mayor or by an official or body to which the Municipal Legislature delegates authority in conformity with the Law No. 81 of August 30, 1991, as amended, known as *Autonomous Municipalities Act of the Commonwealth of Puerto Rico* (Act No. 81). In governmental funds other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.
- ***Unassigned*** – Represent the residual classification for the Municipality's general fund and includes all spendable amounts not contained in the other classifications. In other funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

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

The Municipality reports resources constrained to stabilization as a specified purpose (restricted or committed fund balance in the general fund) only if: (1) such resources meet the other criteria for those classifications, as described above and (2) the circumstances or conditions that signal the need for stabilization are identified in sufficient detail and are not expected to occur routinely. However, the Municipality has not entered into any stabilization-like arrangements, nor has set aside material financial resources for emergencies and has not established formal minimum fund balance amounts as of and for the fiscal year ended June 30, 2012.

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When an expenditure is incurred for purposes for which amounts are available in multiple fund balance classifications, the Municipality uses restricted resources first, and then unrestricted resources. Within unrestricted resources, the Municipality generally spends committed resources first, followed by assigned resources, and then unassigned resources.

p) Interfund Activities

The Municipality has the following types of reciprocal and non-reciprocal inter-fund activities recorded among governmental funds in the accompanying GFFS:

- **Inter-fund loans** – Represent resources (assets) provided by one governmental fund to other governmental fund with a requirement and commitment for repayment (reimbursement), which are recorded as “*due from*” in the lender governmental fund and “*due to*” in the borrower governmental fund. For amounts not expected to be collected, inter-fund receivables/payables are reduced to their estimated realizable (settlement) value, and the portion of the inter-fund loan that is not expected to be repaid is reported as a “*transfer-in*” from the governmental fund that provided the loan.
- **Inter-fund transfers (transfers-in/(out))** – Represent flows of assets (permanent reallocation of financial resources among governmental funds) without equivalent flows of assets in return and without a requirement for repayment. Transfers are reported as “*other financing uses*” in the governmental fund making transfers and as “*other financing sources*” in the governmental fund receiving transfers.
- **Inter-fund reimbursements** – Represent repayments (reimbursements) from the governmental fund responsible for particular expenditures or expenses to the governmental fund that initially paid for them.

In the GFFS, inter-fund activity has not been eliminated, as permitted by GAAP.

q) Use of Estimates

The preparation of the accompanying basic financial statements in conformity with GAAP requires management to make significant 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 basic financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

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r) Future Adoption of Accounting Pronouncements

The GASB has issued the following standards that have effective dates after June 30, 2012:

- GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements* (GASB No. 60). The objective of this Statement is to improve financial reporting by addressing issues related to service concession arrangements (SCAs), which are a type of public-private or public-public partnership. This Statement is effective for periods beginning after December 15, 2011.
- GASB Statement No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34* (GASB No. 61). The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The requirements of Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those Statements. This Statement is effective for periods beginning after June 15, 2012.
- GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and IACPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements; 1) Financial Accounting Standard Board (FASB) Statements and interpretations, 2) Accounting Principles Board Opinions, 3) Accounting Research Bulletins of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. This Statement is effective for periods beginning after December 15, 2011.
- GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011.
- GASB Statement No. 65, *Previously Reported as Assets and Liabilities*. The objective of this Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012.

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- GASB Statement No. 66, *Technical Corrections-2012-an amendment of GASB Statements No. 10 and No. 62 (Issued 03/12)*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012.
- GASB Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25 (Issued 06/12)*. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. This Statement replaces the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 25 and 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement and to defined contribution plans that provide postemployment benefits other than pensions.
- GASB Statement No. 68 *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27 (Issued 06/12)*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. This Statement is effective for fiscal years beginning after June 15, 2014.
- GASB Statement No. 69 *Government Combinations and Disposals of Government Operations (Issued 01/13)*. This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term government combinations include a variety of transactions referred to as mergers, acquisitions, and transfers of operations. The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis.

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- GASB Statement No. 70 *Accounting and Financial Reporting for Nonexchange Financial Guarantees (Issued 04/13)*. The objective of this Statement is to improve accounting and financial reporting by state and local governments that extend and receive nonexchange financial guarantees. The provisions of this Statement are effective for reporting periods beginning after June 15, 2013. Earlier application is encouraged.

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

2. Deposits

The Municipality maintains its deposits in various commercial banks located in Puerto Rico and the Government Development Bank for Puerto Rico (GDB). Proceeds from all bonds and the funds related to certain federal grant awards are required by law to be held with GDB.

On July 1, 2004, the Municipality adopted the provisions of GASB Statement No. 40 (GASB No. 40), *Deposit and Investment Risk Disclosure, an Amendment to GASB Statement No. 3*. This statement requires that state and local governments disclose essential risk information about deposits and investments. The disclosure requirements cover four main areas: (1) credit risk, (2) interest rate risk, (3) custodial credit risk, (4) foreign exchange exposure.

- **Credit risk** – This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In compliance with the laws and regulations of the Commonwealth, the Municipality has adopted, as its custodial credit risk policy, the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*. Accordingly, the Municipality is only allowed to invest its obligations of the Commonwealth, obligations of the United States of America, certificates of deposit, commercial paper, bankers' acceptances or in pools of obligations of the Municipalities of Puerto Rico, which are managed by GDB. According to the aforementioned investment guidelines, the Municipality is not allowed to invest in marketable securities or any other type of investments for which credit risk exposure may be significant. Therefore, the Municipality's management has concluded that the credit risk related to any possible loss related to defaults by commercial banks on the Municipality's deposits is considered low at June 30, 2012.
- **Interest rate risk** – This is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Municipality manages its exposure to declines in fair values by: (1) not including debt investments in its investments portfolio at June 30, 2012, (2) limiting the weighted average maturity of its investments to periods of three months or less and (3) keeping most of its banks deposits in interest bearing accounts generating interest at prevailing market rates. At June 30, 2012, the interest rate risk associated with the Municipality's cash and cash equivalent is considered low.

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- Custodial credit risk** – In the case of deposits, this is the risk that in the event of a bank failure, the Municipality’s deposits may not be recovered. Pursuant to the *Statement of Investment Guidelines for the Government of the Commonwealth of Puerto Rico*, the balances deposited in commercial banks by the Municipality are insured by the Federal Deposit Insurance Corporation (FDIC), generally up to a maximum of \$250,000 per depositor. In addition, public funds deposited in commercial banks by the Municipality are fully collateralized for the amounts deposited in excess of the federal depository insurance. All securities pledged as collateral are held in the Municipality’s name by the agents of the Commonwealth’s Secretary of Treasury. Deposits of GDB, amounting to \$6,892,658 at June 30, 2012, are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2012. It is management’s policy to only maintain deposits in banks affiliated to FDIC to minimize the custodial credit risk, except for GDB. Therefore, the Municipality’s management has concluded that at June 30, 2012, the custodial credit risk associated with the Municipality’s cash and cash equivalents is considered low.
- Foreign exchange risk** – This is the risk that changes in exchange rates will adversely affect the value of an investment or a deposit. According to the aforementioned investment guidelines, adopted by the Municipality, the Municipality is prevented from investing in foreign securities or any other types of investments for which foreign exchange risk exposure may be significant. Accordingly, management has concluded that the foreign exchange risk related to the Municipality’s deposits is considered low at June 30, 2012.

The Municipality’s bank balance of deposits with financial institutions is categorized to provide an indication of the level of collateral risk assumed by the Municipality at June 30, 2012. Risk categories are described as follows:

	General fund	Legislative Joint resolutions Fund	Capital improvement bonds fund	Debt service fund	Other nonmajor fund	Total government al funds
Cash in commercial banks	\$ 359,560	\$ 334,605	-	-	\$ 360,120	\$ 1,054,285
Cash in GDB, as fiscal agent	221,014	-	1,804,441	4,738,674	128,529	6,892,658
Total carrying amount of deposits	<u>\$ 580,574</u>	<u>\$ 334,605</u>	<u>\$ 1,804,441</u>	<u>\$ 4,738,674</u>	<u>\$ 488,649</u>	<u>\$ 7,946,943</u>

3. Municipal License Taxes

The Municipality is authorized by Law No. 81 to impose and collect municipal license taxes on all trade or business activities operated by any natural or legal person within the territorial area of Santa Isabel. This is a self-assessed tax generally based on the business volume measured by gross sales. The Municipality establishes the applicable tax rates. At June 30, 2012, the municipal tax rates imposed by the Municipality were 1.50% for financing institutions and 0.30% for other types of taxpayers. Any taxpayers that have been granted with partial tax exemptions under any of the

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incentive tax laws of the Commonwealth ultimately pay municipal license taxes at reduced tax rates, generally between 60% and 90% under standard rates.

Each taxpayer must assess his/her corresponding municipal license tax by declaring his/her volume of business through a tax return to be filed every April 15 based on the actual volume of business generated in the preceding calendar year.

Taxpayers with a sales volume of \$3 million or more must include audited financial statements with their tax returns. The tax can be paid by the taxpayer in two equal installments due on July 15 and January 15, subsequent to the filing of the declaration.

The first installment of the tax covers the six-month period ended December 31, subsequent to the filing date of the declaration, while the second installment of the tax covers the six-month period ended June 30 of the subsequent calendar year. If a taxpayer elects to pay the tax in full on the filing date of the declaration (generally April 15), a 5% discount is granted automatically on the total tax amount due.

Any municipal license taxes collected in advance (that is, pertaining to a future period) are recorded as deferred revenues. Deferred municipal license tax revenues recorded in the accompanying GWFS and GFFS amounted to \$1,057,606 at June 30, 2012, which represents municipal licenses collected in advance for the taxable year 2012-2013.

4. Sales Taxes

The Municipality is authorized by Law No. 117 of July 4, 2006, as amended by Law No. 80 of July 29, 2007, to impose and collect sales and uses taxes of one point five (1.5) percent to substantially all products and services sold or provided within the territorial limits of the Municipality. The mentioned Laws establish the applicable tax rate.

At June 30, 2012, the municipal sales and uses tax rate imposed by the Municipality was 1.50, from which the Municipality collect one (1) percent, and the Puerto Rico Secretary of the Treasury collect the remaining point five (.5) percent without including food and food ingredients as defined in Section 2301(a) of the Act No. 107, on behalf of the Municipality.

The point five (.5) percent collected by the Puerto Rico Treasury Department and belonging to the Municipality it is distributed through three separate funds: municipal development fund (up to .2%, at the discretion of the Municipality), municipal redemption fund (from .2% to .4%, at the discretion of the Municipality) and municipal improvements fund (.1%). The Municipality has elected to restrict a portion of the sales tax amounting .4% for the payment of long-term debt and is recorded in the debt service fund. The remaining portion is recorded in the general fund since is available for general operating purposes.

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The tax collected by merchants during a given month is due and must be paid accompanied by a sales and use tax return to the Municipality and to the Puerto Rico Treasury Department on or before the 10th day of the following month.

The resources collected by the Municipality due to this tax assessment will be used in local activities like improvements in health services, improvements in the control and management of solid waste disposal and recycling programs, public improvements, improvements of public safety, and maintenance of all public facilities of the Municipality.

The sales and use tax receivable is recognized as revenue when it becomes measurable and available base on actual collection during the 30 days following the fiscal year-end related to sales and use tax returns due before year end.

Sales and use tax receivable in the general and debt service funds at June 30, 2012, of \$130,116 and \$76,958, respectively, represent actual collection during the 30 days following the fiscal year-end related to sales and use tax returns due before year end.

5. Property Taxes

The Municipality is authorized by Law No. 81 to impose and collect property taxes from any natural or legal person that, at January 1 of each calendar year: (1) is engaged in trade or business and is the owner of personal or real property used in trade or business or (2) owns residential real property with a value in excess of \$15,000 (at 1957 estimated market prices).

The Municipal Revenue Collection Center (CRIM, by its Spanish acronym) is a governmental entity not related to the Municipality which is responsible for the billings and collections of real and personal property taxes on behalf of the Municipality and all other municipalities in the Commonwealth of Puerto Rico. Prior to the beginning of each fiscal year, CRIM informs to the Municipality the estimated amount of property taxes expected to be collected for the ensuing fiscal year. Throughout the fiscal year, CRIM advances funds (estimated collections) to the Municipality based on the initial estimated (forecasted) collection amounts for the fiscal year. 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 the property tax amounts actually collected from taxpayers on behalf of the Municipality during the fiscal year. This settlement has to be completed on a final basis not later than December 31 following the fiscal year end. If in any given fiscal year, CRIM remits to the Municipality property tax advances that are less than the property taxes actually collected by CRIM on behalf of the Municipality, then CRIM will increase the amount of the monthly property tax advances during for the next fiscal year. However, if advances exceed the amount actually collected by CRIM, then CRIM will reduce the amount of the monthly property tax advances during the next fiscal year.

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Personal property taxes are self-assessed by taxpayers every year using the book value of personal property assets owned by the taxpayer at January 1 (assessment date) and reporting such taxable value through a personal property tax return filed on May 15 subsequent to the assessment date. The total personal property tax rate in force at June 30, 2012 was 8.53 percent (of which taxpayers pay 8.33 percent and the remaining 0.20 percent is paid by the Department of Treasury, as a subsidy).

Real property taxes are assessed by CRIM. The assessment on real property is made every January 1 and is based on estimated current values of the property, deflated to 1957 market prices. The total real property tax rate in force at June 30, 2012 was 10.53 percent (of which 10.33 percent is paid by taxpayers and the remaining 0.20 percent is also paid by the Department of Treasury, as a subsidy).

Residential real property occupied by its owner (not engaged in trade or business) is exempt from property taxes only on the first \$15,000 of the assessed value (at 1957 market prices). For exempt amounts, the Department of Treasury assumes the payment of the basic tax (4.00 percent and 6.00 percent for personal and real property, respectively), except for property assessed for less than \$3,500 (at 1957 market prices), for which no payment is made by the Department of Treasury.

According to Law No. 81, included within the total personal and real property tax rates of 8.53 percent and 10.53 percent, respectively, there is a levy of an annual special tax of 1.03 percent of the assessed value of all real and personal property not exonerated from taxation. This special tax is levied by the Commonwealth of Puerto Rico but is collected by CRIM. Collections of this special tax are directly remitted by CRIM to the debt service fund of the Commonwealth of Puerto Rico, for the payment of the general long-term debt of the state government.

In addition, included within the total personal and real property tax rates of 8.53 percent and 10.53 percent, respectively, there is a portion of the tax rate in the amount of 1.75 percent that is restricted for the Municipality's debt service requirements of bonds. Such amounts are recorded in the Municipality's debt service fund.

The portion of the property taxes recorded in the general fund is used to finance the operating activities of the Municipality, including the payment of: (1) the insurance premiums acquired through the Puerto Rico Department of Treasury, (2) the monthly contributions to CRIM, which are statutorily required as the Municipality's share of CRIM's operating expenses, (3) statutory contributions to the Puerto Rico Health Services Administration (PRHSA), as the Municipality's share of the cost of the public health insurance coverage provided to qualifying low-income citizens, (4) certain notes payable to CRIM and to the Puerto Rico Department of Treasury and, (5) certain amounts due to certain agencies and component units of the Commonwealth, which are recorded within intergovernmental payables in the accompanying GWFS and GFFS. The 0.20 percent of unrestricted personal and real property taxes paid by the Puerto Rico Department of Treasury as a subsidy is recorded in the Municipality's general fund.

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The Additional Lottery System of the Commonwealth of Puerto Rico (the Additional Lottery) is an operational unit reported as an enterprise fund in the Commonwealth of Puerto Rico's basic financial statements, which currently operates several betting alternatives to the citizens of Puerto Rico. The Additional Lottery is required every fiscal year to distribute a portion of its excess of revenues over expenses as follows:

- Thirty five percent of its net earnings (defined as the excess of revenues over expenses less an amount earmarked for the Fund for Rent and Home Improvement Subsidy Program for the Low-Income Qualifying Elderly) is earmarked to the municipalities of the Commonwealth of Puerto Rico, of which a maximum of \$26 million, on an annual basis, is distributed to the Municipal Equalization Fund held by CRIM to cover operating expenses and permanent improvements of the municipalities.
- An additional amount not exceeding \$16 million, on an annual basis, is distributed to the Municipal Equalization Fund, provided it is within the thirty-five percent corresponding to the municipalities of the Commonwealth of Puerto Rico. When the accumulated municipal appropriations from the municipalities' Puerto Rico Health Reform are covered up to June 30, 1997, these resources will be assigned to PRHSA.

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6. Intergovernmental Receivables and Payables

Intergovernmental receivables and payables recorded in the accompanying GWFS and GFFS are as follows:

	General Fund	Other governmental funds	Total governmental funds	Statement of net assets
<i>Intergovernmental receivables:</i>				
Grants and contributions:				
Puerto Rico Department of Labor – Act. No. 52	\$ -	\$ 109,169	\$ 109,169	\$ 109,169
Puerto Rico Office of the Commissioner of Municipal Affairs	-	326,738	326,738	326,738
Puerto Rico Treasury Department – Christmas bonus	123,534	-	123,534	123,534
Puerto Rico Municipal Revenue Collection Center	437,382	-	437,382	437,382
Others	-	106,284	106,284	106,284
Total intergovernmental receivables	<u>\$ 560,916</u>	<u>\$ 542,191</u>	<u>\$ 1,103,107</u>	<u>\$ 1,103,107</u>
<i>Intergovernmental payables:</i>				
Puerto Rico Treasury Department	\$ 3,685	\$ -	\$ 3,685	\$ 3,685
Employees Retirement System of the Government of the Commonwealth of Puerto Rico	86,751	-	86,751	86,751
Puerto Rico Department of Labor	329,461	-	329,461	329,461
Puerto Rico Aqueduct and Sewer Authority	402,048	-	402,048	402,048
Puerto Rico Energy Power Authority	22,679	-	22,679	22,679
Social Security Administration	39,886	-	39,886	39,886
Puerto Rico General Services Administration	2,080	-	2,080	2,080
Commonwealth of Puerto Rico Employees Association	30,933	-	30,933	30,933
Total intergovernmental payables	<u>\$ 917,523</u>	<u>\$ -</u>	<u>\$ 917,523</u>	<u>\$ 917,523</u>

Intergovernmental receivables and payables represent the pending settlements of the aforementioned intergovernmental transactions.

The amount due from Puerto Rico Department of Treasury – Christmas bonus (\$123,534) and (\$437,382) from Puerto Rico Municipal Revenue Collection Center are recorded as deferred revenues in the governmental funds statements (general fund) since is not available as required by modified accrual basis of accounting.

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7. Interfund Balances

On July 1, 2003 the Municipality adopted the provisions of Statement No. 38, Certain Financial Statement Note Disclosures, issued by the Governmental Accounting Standards Board. This statement requires the disclosure of the flow of resources between funds and to assess the collectibility of interfund balances. Interfund balances at June 30, 2012 consisted of the following:

Due/advances from:				
Due/advances to:	General fund	State legislative joint resolutions fund	Other governmental funds	Total governmental funds
Major governmental funds:				
General fund	\$ -	1,054,695	30,074	\$ 1,084,769
Non-major governmental funds:	204,045	-	405	204,450
Total	\$ 204,045	1,054,695	30,479	\$ 1,289,219
Transfers out:				
Transfers in:	General fund	Total governmental funds		
Major governmental funds:				
Debt service fund	\$ 181,987	\$ 181,987		
Total	\$ 181,987	\$ 181,987		

The principal purposes of inter-fund receivables and payables are to recognize in the outstanding balance of the loans granted, the effect of the practice of pooling cash in the a current account, and to temporarily cover the payroll and other operating costs of several federally, and local and state funded programs.

The principal purposes of inter-fund transfers are to make a routinary transfer of resources from the general fund to the debt service fund to cover the principal and interest payment on certain bond. These debt service payments were made on January and July 2012.

Inter-fund receivables and payables represent the pending settlements of the aforementioned transfers at June 30, 2012.

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8. Capital Assets

Capital assets activity of the governmental activities for the fiscal year ended June 30, 2012 was as follow:

	Cost basis at beginning of fiscal year	Additions	Reductions/ Reclassifications	Cost basis at end of fiscal year
<i>Cost basis:</i>				
Capital assets, not being depreciated:				
Land	\$ 1,433,191	\$ -	\$ -	\$ 1,433,191
Construction in progress	604,056	-	604,056	-
Total capital assets, not being depreciated	<u>2,037,247</u>	<u>-</u>	<u>604,056</u>	<u>1,433,191</u>
Capital assets, being depreciated:				
Buildings, structures and buildings improvements	19,782,983	604,056	-	20,387,039
Infrastructure	5,283,512	-	-	5,283,512
Land improvements	62,800	-	-	62,800
Licensed vehicles	2,509,805	199,544	-	2,709,349
Machinery and equipment	1,909,323	104,410	27,758	1,985,975
Total capital assets, being depreciated	<u>29,548,423</u>	<u>908,010</u>	<u>27,758</u>	<u>30,428,675</u>
Total cost basis of capital assets	<u>\$ 31,585,670</u>	<u>\$ 908,010</u>	<u>\$ 631,814</u>	<u>\$ 31,861,866</u>
	Accumulated Depreciation at beginning of fiscal year	Additions	Reductions/ Reclassifications	Accumulated Depreciation at end of fiscal year
Accumulated depreciation:				
Buildings, structures and buildings improvements	\$ 3,281,397	\$ 425,550	\$ -	\$ 3,706,947
Infrastructure	1,838,538	185,849	-	2,024,387
Land improvements	8,100	1,130	-	9,230
Licensed vehicles	1,943,716	168,075	-	2,111,791
Machinery and equipment	880,670	168,525	27,758	1,021,437
Total accumulated depreciation	<u>7,952,421</u>	<u>949,129</u>	<u>27,758</u>	<u>8,873,792</u>
Net capital assets, governmental activities	<u>\$ 23,633,249</u>	<u>\$ (41,119)</u>	<u>\$ 604,056</u>	<u>\$ 22,988,074</u>

The Municipality did not have complete and accurate accounting records of capital assets at June 30, 2012.

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Depreciation and amortization expense of governmental activities for the fiscal year ended June 30, 2012 was charged to functions/programs in the accompanying statement of activities as follows:

General government	\$ 175,014
Public safety	79,500
Welfare and housing assistance	7,525
Culture, recreation, and education	211,007
Health and sanitation	4,750
Urban and economic development	471,333
Total depreciation and amortization expense	<u>\$ 949,129</u>

9. Deferred Revenues

At June 30, 2012, deferred revenues recorded in the GWFS and the governmental fund financial statements are as follows:

	General fund	Other non-major fund	Total governmental funds	Statement of net assets
<i>Unearned revenues:</i>				
Municipal licenses	\$ 1,057,606	\$ -	\$ 1,057,606	\$ 1,057,606
Intergovernmental grants and contributions	-	177,751	177,751	177,751
Total unearned revenues	<u>\$ 1,057,606</u>	<u>\$ 177,751</u>	<u>\$ 1,235,357</u>	<u>\$ 1,235,357</u>
<i>Unavailable revenues:</i>				
CRIM Final Settlement	\$ 437,382	\$ -	\$ 437,382	\$ -
Intergovernmental grants and contributions	123,534	-	123,534	-
Total unavailable revenues	<u>560,916</u>	<u>-</u>	<u>560,916</u>	<u>-</u>
Total deferred revenues	<u>\$ 1,618,522</u>	<u>\$ 177,751</u>	<u>\$ 1,796,273</u>	<u>\$ 1,235,357</u>

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10. Long-Term Obligations

The general long-term debt activity for the fiscal year ended June 30, 2012 is as follows:

	Balance at June 30, 2011	Borrowings or Additions	Payments or Deductions	Balance at June 30, 2012	Due Within One Year
Bonds and bond anticipation notes payables	\$23,869,500	\$ -	\$ 597,000	\$23,272,500	\$ 595,000
Notes payable to					
Puerto Rico Treasury Department					
Financing agreement to settle two legal demands	480,386	-	192,155	288,231	192,155
CRIM:					
Advances over collections through fiscal year 2000	486,475	-	11,292	475,183	12,003
Act No. 146 -Financing of delinquent property tax accounts sold	439,676	-	20,937	418,739	20,937
LIMS Reimbursement	11,795	-	11,795	-	-
Final Settlement – Fiscal Year 2009-2010	26,704	-	26,704	-	-
Compensated absences	1,363,635	986,861	833,313	1,517,183	950,000
Estimated landfill closure and post closure care costs	3,420,000	-	160,000	3,260,000	1,140,000
Christmas bonus	168,947	265,969	168,947	265,969	265,969
Total	\$ 30,267,118	\$ 1,252,830	\$ 2,022,143	\$ 29,497,805	\$ 3,176,064

Historically, the general fund has been used to liquidate the notes payable to CRIM, the Puerto Rico Department of Treasury, compensated absences and any other long-term liabilities other than bonds.

o) Debt Limitation

The Municipal Legislature is legally authorized to approve the contracting of debts of the Municipality. Nevertheless, the laws and regulations of the Commonwealth of Puerto Rico also provide that:

- Direct obligations of the Municipality (evidenced principally by bonds) are backed by the full faith, credit and taxing power of the Municipality; and
- Direct obligations are not to be issued by the Municipality if the amount of the principal of, and the interest on, such bonds and bond anticipation notes (and on all bonds and notes issued thereafter) which are payable in any fiscal year, together with any amount paid by the Municipality in the preceding fiscal year on account of bonds or bond anticipation notes guaranteed by the Municipality, exceed 10 percent of the total assessed value of the property located within the Municipality plus the balance of the ad valorem taxes in the debt service fund, for bonds payable and bond anticipation notes to be repaid with the proceeds of property taxes restricted for debt service.

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p) Bonds Payable

The Municipality issues general obligation and public improvement serial bonds to finance the acquisition, construction and improvement of capital assets, as well as, to finance certain operating needs, including the payment to suppliers in certain circumstances.

The laws and regulations of the Commonwealth provide that the Municipality's public debt will constitute a first claim on the available revenue of the Municipality. Public debt is composed of bonds payable. The good faith, credit and taxing power of the Municipality are irrevocably pledged for the prompt payment of the principal and interest of bonds.

As more fully described in Note 5, the Municipality levies an annual additional special property tax of 1.75 percent of the assessed value of personal and real property. The proceeds of this additional special tax are deposited in a sinking fund established at the Government Development Bank for Puerto Rico, fiscal agent, whereby sufficient funds are set aside to redeem the bonds payable of the Municipality in minimum annual and semiannual principal and interest payments. The collections of this special tax are recorded in the Municipality's debt service fund.

As more fully described in Note 4, the Municipality impose and collect sales and uses taxes of one point five (1.5) percent, of which the Municipality has elected to restrict a portion amounting .4% for the payment of long-term bonds. The collections of this sales and use tax are recorded in the Municipality's debt service fund.

For financial reporting purposes, the outstanding balances of bonds represent the total principal to be repaid. Bonds payable is composed as follows at June 30, 2012:

<u>General and Special Obligations:</u>	<u>Outstanding Amount</u>
\$1,850,000 rent bond series of 2003 payable in annual installments ranging from \$30,000 to \$140,000 through July 2027, interest ranging 2.43% to 6.50%	\$ 1,480,000
\$730,000 rent bond series of 2003 payable in annual installments ranging from \$10,000 to \$55,000 through July 2027, interest ranging 2.43% to 6.50%	585,000
\$33,000 rent bond series of 1994 payable in annual installments ranging from \$1,000 to \$2,000 through January 2018, interest at 4.5%	12,000
\$205,000 rent bond series of 1997 payable in annual installments ranging from \$5,000 to \$20,000 through July 2022, interest ranging 4.87% to 6.56%	135,000
\$215,000 rent bond series of 1994 payable in annual installments ranging from \$5,000 to \$15,000 through January 2018, interest at 4.5%	79,000

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<u>General and Special Obligations:</u>	<u>Outstanding Amount</u>
\$361,000 rent bond series of 2003 payable in annual installments ranging from \$9,000 to \$25,000 through July 2019, interest at 5.0%	94,000
\$230,000 rent bond series of 2003 payable in annual installments ranging from \$9,000 to \$22,500 through July 2019, interest ranging 4.50% to 6.00%	148,500
\$630,000 general obligations bonds series of 1997 payable in semi annual installments ranging of \$10,000 to \$60,000 through July 2020, interest from 4.7% to 6.63%	375,000
\$755,000 general obligation bonds series of 2001 payable in semi annual installments ranging of \$5,000 to \$65,000 through July 2025, interest ranging from 5% to 7.5%	580,000
\$185,000 general obligation bonds series 2004 payable in semi annual installments ranging from \$5,000 to \$ 15,000 through July 2028, interest ranging 5.0% to 6.5%	145,000
\$185,000 general obligation bonds series 2004 payable in semi annual installments ranging from \$5,000 to \$ 15,000 through July 2028, interest ranging 5.0% to 6.0%	145,000
\$300,000 general obligation bond series of 2001 payable in annual installments ranging of \$7,000 to \$21,000 through July 2029, interest at 4.75%	238,000
\$1,410,000 general obligation bond series of 2006 payable in annual installments ranging of \$40,000 to \$115,000 through July 2025, interest ranging 5.32 to 5.5%	1,130,000
\$2,690,000 general obligation bond series of 2007 payable in annual installments ranging of \$40,000 to \$225,000 through July 2031, interest at 5.5%	2,455,000
\$210,000 general obligation bond series of 2007 payable in annual installments ranging of \$25,000 to \$35,000 through July 2015, interest at 5.5%	70,000

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<u>General and Special Obligations:</u>	<u>Outstanding Amount</u>
\$745,000 general obligation bond series of 2008 payable in annual installments ranging of \$20,000 to \$70,000 through July 2027, interest ranging 2.43% to 7.0%	665,000
\$5,356,000,000 general obligation bond series of 2008 payable in annual installments ranging of \$85,000 to \$456,000 through July 2032, interest ranging 2.43% to 7.50%	5,081,000
\$810,000 general obligation bond series of 2010 payable in annual installments ranging of \$5,000 to \$70,000 through July 2034, interest ranging 4.75% to 6.50%	795,000
\$6,500,000 general obligation bond series of 2010 payable in annual installments ranging of \$60,000 to \$915,000 through July 2034, interest ranging 6.00% to 7.00%	6,380,000
\$2,720,000 special obligation bond series of 2010 payable in annual installments ranging of \$40,000 to \$220,000 through July 2035, interest ranging 6.00% to 7.00%	2,680,000
Total bonds	<u><u>\$ 23,272,500</u></u>

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

2013	\$ 595,000	\$ 970,941	\$ 1,565,941
2014	643,000	1,499,918	2,142,918
2015	641,000	1,693,232	2,334,232
2016	689,000	1,413,728	2,102,728
2017	711,000	1,367,407	2,078,407
2018-2022	4,125,500	6,019,861	10,145,361
2023-2027	5,322,000	4,646,849	9,968,849
2028-2032	6,485,000	2,586,810	9,071,810
2033-2038	4,061,000	433,137	4,494,137
Totals	<u>\$ 23,272,500</u>	<u>20,631,883</u>	<u>\$ 43,904,383</u>

c) *Notes Payable to Puerto Rico Treasury Department*

Loan for payment of legal settlement - On December 1, 2003 the Municipality obtained a loan from the Puerto Rico Treasury Department to pay a legal settlement. The face amount of the loan was \$1,921,548 at no interest. This note has an imputed interest rate of 5.00% and was originally recorded at its present value of \$1,509,718, net of an unamortized discount of \$411,830, at inception. At June 30, 2012, the outstanding balance of this note amounted to \$288,231. The principal and discount amortization maturities are as follows:

<u>Year ending June 30,</u>	<u>Principal amortization</u>	<u>Discount amortization</u>	<u>Total</u>
2013	\$ 178,828	13,327	\$ 192,155
2014	96,076	-	96,076
Total	<u>\$ 274,904</u>	<u>13,327</u>	<u>\$ 288,231</u>

d) *Notes Payable to CRIM*

Act No. 42 – Act No. 42 of January 26, 2000 was enacted to authorize CRIM to enter into a financing agreement of up to \$200 million, for a term not exceeding 30 years. The financing agreement allows for the financing of a debt that the municipalities of Puerto Rico have with CRIM, arising from the final settlements of property tax advances versus actual collections through fiscal year 2000. The amounts that the municipalities will collect from the additional property taxes resulting from the increases in the subsidy from the Commonwealth to the municipalities are assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238 of August 15, 1999.

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assigned through this law to repay such loan. The increase in this subsidy was the result of the Public Law No. 238 of August 15, 1999.

In addition, on February 12, 2003, the Municipality entered into a repayment agreement with GDB and CRIM to pay off the remaining \$559,133 of excess of property tax advances through fiscal year 2000 and 2001. CRIM retains the principal and interest from the property tax advances of the Municipality. The amounts retained by CRIM are remitted to GDB on July 1 of each year through July 1, 2032. The repayment agreement bears interest at variable rates determined by GDB. The outstanding principal balances of the note payable to CRIM amounted \$475,183, at June 30, 2012. The principal and interest maturities are as follows:

<u>Year ending</u> <u>June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 12,003	\$ 29,218	\$ 41,221
2014	12,756	28,465	41,221
2015	13,558	27,663	41,221
2016	14,410	26,811	41,221
2017	15,315	25,906	41,221
2018-2022	71,508	93,377	164,885
2023-2027	117,749	88,358	206,107
2028-2032	159,690	46,415	206,105
2033-2037	58,194	3,636	61,830
Total	<u>\$ 475,183</u>	<u>369,849</u>	<u>\$ 845,032</u>

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Financing of delinquent property tax accounts sold – On April 22, 2002, the Municipality entered into a financing agreement with CRIM in the amount of \$688,000 for the payment of delinquent property tax account sold to private investors. The financing agreement in the form of a line of credit bearing interests at 6.50% during the first 5 years, and variable interests 125 points over LIBOR rate during the next 25 years. At June 30, 2012, the outstanding principal balances amounted to \$418,739. The principal and interest maturities are as follows:

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 20,937	\$ 26,046	\$ 46,983
2014	20,937	24,744	45,681
2015	20,937	23,442	44,379
2016	20,937	22,138	43,075
2017	20,937	20,836	41,773
2018-2022	83,748	70,324	154,072
2023-2027	104,685	58,602	163,287
2028-2032	104,685	26,046	130,731
2033-2037	20,936	1,302	22,238
Total	<u>\$ 418,739</u>	<u>\$ 273,480</u>	<u>\$ 692,219</u>

e) Compensated Absences

At June 30, 2012, the government-wide statement of net assets – governmental activities includes a liability amounting \$1,517,183, of which \$850,767 represents accrued sick leave benefits, and \$666,416 represents accrued vacation benefits, representing the Municipality’s commitment to fund such costs from future operations.

11. Employees Retirement System

o) Plan Description

The Municipality’s employees participate in the Employees’ Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS), a cost-sharing multi-employer (as related to the Municipality’s reporting entity) defined pension plan established by the Commonwealth. Substantially all full-time employees of the Commonwealth and substantially all municipalities are covered by ERS under the terms of Public Act No. 447 of May 15, 1951, as amended (Act No. 447). All regular and temporary employees of the Municipality become plan members of ERS at the date of employment, while it is optional for officers appointed.

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ERS members, other than those joining it after March 31, 1990, are eligible for the benefits described below:

- ***Retirement Annuity***

ERS members are eligible for a retirement annuity upon reaching the following age:

Policemen and firemen:	Other employees:
50 with 25 years of credited service	55 with 25 years of credited service
58 with 10 years of credited service	58 with 10 years of credited service

ERS members are eligible for monthly benefit payments determined by the application of the stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the highest 36 months of compensation recognized by ERS. The annuity, for which a member is eligible, is limited to a minimum of \$300 per month and a maximum of 75 percent of the average compensation.

- ***Merit Annuity***

ERS members are eligible for merit annuity with a minimum of 30 years or more of credited service. The annuity for which the plan member is eligible is limited to a minimum of 65 percent and a maximum of 75 percent of the average compensation.

- ***Deferred Retirement Annuity***

A participating employee who ceases to be an employee of the Municipality after having accumulated a minimum of ten years of credited service qualifies for retirement benefits provided his/her contributions are left in ERS until reaching 58 years of age.

- ***Coordinated Plan***

On the coordinated plan, by the time the employee reaches 65 years old and begins to receive social security benefits, the pension benefits are reduced by the following:

- (a) \$165 per month, if retired with 55 years of age and 30 years of credited service.
- (b) \$110 per month, if retired with less than 55 years of age and 30 years of credited service.
- (c) All other between \$82 and \$100 per month.

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(d) Disability annuities under the coordinated plan are also adjusted at age 65 and in some cases can be reduced over \$165 per month.

- ***Non-Coordinated Plan***

On the non-coordinated plan the participating employee and does not have any change on the pension benefits upon receiving social security benefits.

- ***Reversionary Annuity***

An ERS member, upon retirement, could elect to receive a reduced retirement annuity giving one or more benefit payments to his/her dependents. The life annuity payments would start after the death of the retiree for an amount not less than \$240 per year or greater than the annuity payments being received by the retiree.

- ***Occupational Disability Annuity***

A participating employee, who as a direct result of the performance of his/her occupation is totally and permanently disabled, is eligible for a disability annuity of 50 percent of the compensation received at the time of the disability.

- ***Nonoccupational Disability Annuity***

A participating employee, totally and permanently disabled for causes not related to his/her occupation and with no less than 10 years of credited service, is eligible for an annuity of 1.50 percent of the average compensation of the first 20 years of credited services, increased by 2 percent for every additional year of credited service in excess of 20 years.

- ***Death Benefits***

Occupational:

(a) **Surviving spouse** – annuity equal to 50 percent of the participating employee's salary at the date of the death.

(b) **Children** - \$10 per month for each child, minor or student, up to a maximum benefit per family of \$100.

Nonoccupational:

Beneficiary – the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of the death.

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Post-retirement:

Beneficiary with surviving spouse age 60 or over and a child, 18 or under, up to 30 percent (60 percent, if not covered under Title II of the Social Security Act) (increased to 50 percent effective January 1, 2005) of retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$750.

- ***Refunds***

A participating employee who ceases his/her employment with the Municipality without the right to a retirement annuity has the right to a refund of the contributions to ERS plus any interest earned thereon.

- ***Cost of Living Adjustment for Pension Benefits***

Public Act No. 10 of May 21, 1992 (Act No. 10) provided for increases of 3 percent every three or more years of retirement. Act No. 10 requires further legislation to grant this increase every three years subject to the presentation of actuarial studies regarding its costs and the source of financing. To protect the financial health of ERS, the increase granted during 2001 and the one granted on January 1, 2005 are being financed by the Municipality and the other participating employers.

To avoid any economic impact on ERS, the employers are responsible for contributing to ERS the amounts to cover the benefit payments and the employer and employee contributions with respect to the participants covered until the participants reach the normal retirement age.

- ***Amendment to Act No. 447 effective January 1, 2000 to create a Defined Contribution Plan***

On September 24, 1999, Public Act No. 305, an amendment to Act No. 447, was enacted to establish a defined contribution plan, known as System 2000, to cover employees joining ERS on or after January 1, 2000.

Employees that participated in the original plan as of December 31, 1999, had the opportunity to elect to either stay in the defined benefit plan or transfer to System 2000. Employees that joined the Municipality on or after January 1, 2000, were only 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 is a pool of plan assets, which is invested by the System, together with

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those of the cost-sharing multi-employer defined benefit plan. Neither the Commonwealth nor the Municipality guarantee benefits at retirement age. The annuity is based on a formula which assumes that each fiscal year the employee's contribution (with a minimum of 8.28 percent of the employee's salary up to a maximum of 10 percent) is invested as instructed by the employee in an account which either: (1) earns a fixed rate based on the two-year Constant Maturity Treasury Notes, (2) earns a rate equal to 75 percent of the return of the ERS' investment portfolio (net of management fees), or (3) earns a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability benefits are not granted under System 2000, rather are provided to those participants that voluntarily elect to participate in a private insurance long-term disability program. The employers' contributions (9.28 percent of the employee's salary) with respect to employees under System 2000 will continue and will be used to fund the cost-sharing multi-employer defined benefit plan.

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

Historically, the state government of the Commonwealth of Puerto Rico has reported ERS and System 2000 in its basic financial statements as pension trust funds. Accordingly, the Commonwealth is currently assuming any actuarial deficiency that may exist or arise related to the Municipality's participating employees because ERS does not allocate to the Municipality any actuarial deficiencies pertaining to participating municipal employees. The Municipality is only required by law to make statutory contributions at the rates detailed below.

- ***Recent Amendments to Act No. 447***

The Senate and the House of Representatives of the Commonwealth of Puerto Rico have the authority for establishing or amending the contribution requirements of System 2000 by approving the necessary amendments or laws, subject to the final approval of the Governor of the Commonwealth of Puerto Rico.

In June and July 2003, the Governor of the Commonwealth signed three Public Acts that provided the following certain benefits to retirees:

- (a) Increase in minimum monthly pension payments to \$300, effective January 1, 2005.
- (b) Triennial 3 percent increase in all pensions, effective January 1, 2005.
- (c) Increase in widow and/or beneficiaries to 50 percent of the benefit received by the deceased pensioner, effective January 1, 2005.

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June 30, 2012

All the benefits granted will be funded through budgetary assignments in the Municipality's general fund with respect to its retired employees.

The Board of Trustees of ERS approved, effective November 17, 2003, an increase in the amount granted on personal loans to participating employees from \$3,000 to \$5,000.

p) Funding Policy

The contribution requirement to ERS is established by law and is not actuarially determined. These contributions are as follows:

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Municipality and other employers	9.28 percent of applicable payroll
Employees:	
Coordination plan:	5.78 percent of gross salary up to \$6,600 per year, plus 8.28 percent gross salary in excess of \$6,600.
Supplementation plan:	8.28 percent of gross salary. This is the only choice available to policemen, firemen and mayors

The contribution requirement to System 2000 is also established by law and is not actuarially determined. These contributions are as follows:

Municipality and other employers	9.28 percent of applicable payroll
Employees:	5.78 percent of gross salary up to \$6,600 per year, plus 8.28 percent gross salary in excess of \$6,600.

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COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
June 30, 2012

q) Annual Contribution

The actual combined employer and employee contributions to ERS and System 2000 for the current and past two years, which are equal to the statutory required contributions, are as follows:

<u>Fiscal year ended June 30,</u>	<u>Act No. 447</u>	<u>System 2000</u>	<u>Total</u>
2012	\$ 273,238	\$ 211,525	\$ 484,763
2011	252,897	198,522	451,419
2010	223,420	156,056	379,476
Totals	<u>\$ 749,555</u>	<u>\$ 566,103</u>	<u>\$ 1,315,658</u>

During the fiscal years ended June 30, 2010, 2011, and 2012, the Municipality and the participating employees contributed at least 100 percent of the required contributions to ERS and System 2000. The authority under which obligations to contribute to ERS and System 2000 by the plans' members, employers and other contributing entities (i.e., state or municipal contributions) are established or may be amended by law by the House of Representatives, the Senate and the Governor of the Commonwealth of Puerto Rico.

Readers can obtain copies of the audited basic financial statements (GAAP basis) of ERS and System 2000 by writing to Mr. Hector M. Mayol Kauffmann, Executive Director of the Retirement Systems Administration of the Commonwealth of Puerto Rico (the entity that administers ERS and System 2000) at PO Box 42004, Minillas Station, Santurce, Puerto Rico 00940.

12. Landfill Closure and Postclosure Care Costs Obligations

State and federal laws and regulations require the Municipality to place a final cover on its landfill site when closed and perform certain maintenance and monitoring functions at the landfill site for 30 years after closure. Although closure and postclosure care costs will be paid only near or after the date that the landfill stops accepting waste, the Municipality reports a portion of these closure and postclosure care costs as an operating expense in each period based on landfill capacity used as of each statement of net assets date. The \$3,260,000 reported as landfill closure and postclosure care liability at June 30, 2012, represents the total cost contracted with a private contractor on December 2011 in order to proceed with the closure of the landfill, according to the US Environmental protection Agency Order by Consent RCRA-02-20211-7303. The closing date of the landfill is the year 2013. Actual cost may be higher due to inflation, changes in technology, or changes in regulations.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Basic Financial Statements
June 30, 2012

13. Commitments, Contingencies and Uncertainties

Encumbrances

The Municipality has reported, outstanding encumbrances amounting to \$200,894 in the general fund at June 30, 2012. The Municipality intends to honor these encumbrances, which will continue to be liquidated under the current year's budget during a lapse period that extends into the subsequent fiscal year.

Construction

The Municipality had commitments at June 30, 2012 of approximately \$1,450,000 for the construction, improvements, or renovation of several capital facilities and the capital assets.

Claims and Judgments

The Municipality is defendant in various legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended, persons are allowed to sue the Municipality only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Municipality may provide its officers and employees with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the payment of such judgment.

The Municipality also is a defendant in a number of lawsuits arising principally from claims against the Municipality for alleged improper actions, and other legal matters that arise in the ordinary course of the Municipality's activities. With respects to pending or threatened litigation, the Municipality has reported no liabilities as of June 30, 2012. Management believes, based on the advice of the legal counsel, that the potential claims against the Municipality not covered by insurance will not materially affect the financial resources for its payment.

During fiscal year 2011-2012, the external lawyers did not provide an external confirmation relates to pending or threatened litigations.

Federal Financially Assisted Programs

The Municipality receives financial assistance from the federal government in the form of grants and entitlements. Receipts of grants are generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal law and regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to audit under Circular A-133 of the Office of Management and Budget of the United States of America (OMB Circular A-133). Disallowance as a result of these audits may become liabilities of the Municipality

COMMONWEALTH OF PUERTO RICO
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Notes to Basic Financial Statements
June 30, 2012

14. Fund Balance (Deficit)

As of June 30, 2012, fund balance (deficit) is comprised of the following:

Fund balances (deficit)	General fund	State legislative joint resolutions fund	Capital improvement bonds fund	Debt service fund	Other governmental funds	Total
<i>Restricted for:</i>						
Urban and economic development	\$ 111,746	\$ 1,181,793	\$ 1,509,435	\$ -	\$ -	\$ 2,802,974
Public safety	-	-	-	-	39,424	39,424
Health and sanitation	-	-	-	-	21,381	21,381
Culture and recreation and education	-	-	-	-	67,760	67,760
Welfare and housing assistance	-	-	-	-	59,417	59,417
Debt service	-	-	-	3,801,602	-	3,801,602
<i>Unassigned</i>	(4,012,653)	-	-	-	-	(4,012,653)
Total fund balances (deficit)	\$ (3,900,907)	\$ 1,181,793	\$ 1,509,435	\$ 3,801,602	\$ 187,982	\$ 2,779,905

15. Subsequent Events

On November 2012, the Municipality issued a General Obligation Bond, amounting to \$525,000. The net proceed will be used to carry out certain capital improvements programs authorized by law. The interest rate on the bond is prime rate variable plus 1.50 percent and maturity date is July 1, 2042.

On December 2012 the Municipality's Legislative branch authorized the issuance of \$1,255,000 of general obligation bond principally to finance debts with other governmental entities and suppliers. The interest rate on the bond is prime rate variable plus 1.50 percent and maturity date is July 1, 2042.

On January 2013, the Municipality's Legislature approved a Municipal Ordinance to impose a new tax rates on real and personal property located within the jurisdiction of the Municipality of Juana Diaz. Such new tax rates will be effective at January 1, 2013.

On April 4, 2013, the Legislature of the Commonwealth of Puerto Rico issued Act No. 3, which amends the previously issued Act 447 of 1951 ("Retirement System Act"). This Act make significant changes to the Employees Retirement System of the Commonwealth of Puerto Rico (the "ERS") trust created by Act 447 of May 15, 1951, as amended, to provide pension and other benefits to retired employees of the government of Puerto Rico and its instrumentalities.

On June 30, 2013, the Legislature of the Commonwealth of Puerto Rico issued Act No. 40, which includes amendments to the sales and use tax sections of the Puerto Rico Internal Revenue Code.

End of Notes to Basic Financial statements

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Budgetary Comparison Schedule- General Fund
(See Notes to Budgetary Comparison Schedule)
June 30, 2012

	Budgeted amounts		Actual amounts	Variance with
	Original	Final	(budgetary basis)	final budget – over (under)
Revenues:				
Property taxes	\$ 1,756,851	\$ 2,259,225	\$ 2,245,028	\$ (14,197)
Municipal license taxes	1,632,428	1,632,428	1,469,046	(163,382)
Sales and use taxes	1,920,000	1,920,000	1,610,585	(309,415)
Construction excise taxes	1,302,900	1,302,900	748,521	(554,379)
Intergovernmental grants and contributions	4,687,346	4,687,346	4,796,824	109,478
Interest on deposits	70,000	70,000	101,848	31,848
Charges for services	27,000	27,000	66,927	39,927
Miscellaneous	108,000	108,000	173,780	65,780
Total revenues	<u>11,504,525</u>	<u>12,006,899</u>	<u>11,212,559</u>	<u>(794,340)</u>
Expenditures and encumbrances:				
General government	4,743,573	4,896,624	6,123,865	(1,227,241)
Urban and economic development	4,761,391	4,757,989	5,426,040	(668,051)
Public safety	728,788	726,953	518,547	208,406
Health and sanitation	571,664	569,697	546,437	23,260
Culture, recreation and education	536,610	856,255	714,885	141,370
Welfare and housing assistance	453,274	509,370	472,171	37,199
Total expenditures	<u>11,795,300</u>	<u>12,316,888</u>	<u>13,801,945</u>	<u>(1,485,057)</u>
Revenues over (under)				
expenditures and encumbrances	<u>(290,775)</u>	<u>(309,989)</u>	<u>(2,589,386)</u>	<u>(2,279,397)</u>
Other financing sources (uses):				
Transfer in from other governmental funds	500,000	519,214	-	(519,214)
Transfer out to other governmental funds	(209,225)	(209,225)	(158,237)	50,988
Total other financing sources (uses)	<u>290,775</u>	<u>309,989</u>	<u>(158,237)</u>	<u>(468,226)</u>
Net increase (decrease)				
in fund balance (deficit)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (2,747,623)</u>	<u>\$ (2,747,623)</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Budgetary Comparison Schedule- General Fund
(See Notes to Budgetary Comparison Schedule)
June 30, 2012

Reconciliation of differences:

Sources/inflows of financial resources:

Actual amounts (budgetary basis) "available for appropriations" from the budgetary comparison schedule (including other financing sources)	\$ 11,212,559
Differences - budgetary basis to GAAP:	
Differences in bases of accounting:	
GAAP adjustments to revenues	<u>18,875</u>
Total revenues and other financing sources reported on the statement of revenues, expenditures and changes in fund balances	<u>\$ 11,231,434</u>

Uses/outflows of financial resources:

Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule (including other financing uses)	\$ 13,960,182
Timing differences:	
Current year encumbrances recorded as expenditures for budgetary purposes	(200,894)
Prior year encumbrances recorded as expenditures for GAAP purposes	187,209
Entity differences:	
Non-budgeted transfers to other funds	23,750
Non-budgeted expenditures	<u>793,203</u>
Total expenditures and other financing uses reported on the statement of revenues, expenditures and changes in fund balances	<u>\$ 14,763,450</u>

See accompanying notes to financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Budgetary Comparison Schedule- General Fund
June 30, 2012

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Control

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

The Municipality prepares its annual budget including the operations of the general fund.

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

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

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2012 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2012.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF AGRICULTURE:			
Pass-through State - Department of Education:			
Child and Adult Care Food Program	10.558	N/AV	\$ 48,658
Total U.S. Department of Agriculture			48,658
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Section 8 Housing Choice Voucher	14.871		371,891
Pass-Through State - Office of the Commissioner of Municipal Affairs:			
Community Development Block Grants – State’s Program	14.228	11-FC 10-AB-FC 09-AB-FC 08-AB-FC 07-AB 06-AB-FC 04-AB-FC 03-AB-FC 02-AB 01-FD	1,515,372
Pass-Through State – State Department of Family:			
Homelessness Prevention and Rapid Re-Housing Program (Recovery Act Funded)	14.257	122-2010-000312	127,684
Total U.S. Department of Housing and Urban Development			2,014,947

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Federal Grantor/Pass-through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Entity Identifying Number</u>	<u>Expenditures</u>
U.S. DEPARTMENT OF ENERGY:			
Pass-through State – Office of the Energy Affairs Administration:			
Energy Efficiency and Conservation Block Grant Program (ARRA funded)	81.128	N/AV	<u>64,261</u>
Total U.S. Department of Energy			<u>64,261</u>
U.S. DEPARTMENT OF HOMELAND SECURITY:			
Pass-Through State – Office of the Governor:			
Disaster Grants- Public Assistance	97.036	N/AV	35,301
Hazard Mitigation Grant	97.039	1798-DR-PR	18,750
Pass-Through the Governor’s Office of the Commonwealth of Puerto Rico			
Homeland Security Grant	97.067	N/AV	<u>49,506</u>
Total U.S. Department of Homeland Security			<u>103,557</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICE			
Pass-Through State – Administration of Children and Families:			
Child Care and Development Block Grant	93.575	241-2012-000111	<u>625,002</u>
Total U.S. Department of Health and Human Service:			<u>625,002</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 2,856,425</u>

See notes to the Schedule of Expenditures of Federal Awards

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 – GENERAL

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of **Santa Isabel**, Puerto Rico (Municipality) and is presented on the modified accrual basis. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the general-purpose financial statements. The reporting entity is defined in Note (1) (A) to the general-purpose combined financial statements.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. The accompanying Schedule of Expenditures of Federal Awards is prepared from Municipality's accounting records and is not intended to present financial position or the results of operations.
2. The Municipality in accordance with the terms, records the financial transactions and conditions of the grants, which are consistent with accounting principles generally accepted in the United States of America.
3. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable or when actually paid, whichever occurs first.

NOTE 3 – FEDERAL CFDA NUMBER

The CFDA numbers included in this Schedule are determined based on the program name, review of grant contract information and the Office of Management and Budget's Catalogue of Federal Domestic Assistance.

NOTE 4 – PASS-THROUGH GRANTOR'S NUMBER

State or local government redistribution of federal awards to the Municipality, treated as if they were received directly from the federal government. OMB Circular A-133 requires the schedule to include the name of the pass-through entity and identifying number assigned by the pass-through entity for federal awards received as a sub recipient. Numbers identified as N/AV are not available.

NOTE 5 – MAJOR PROGRAMS

Major programs are identified in the Summary of Auditor's Results Section of the Schedule of Findings and Questioned Costs.

PEDRO C. ORTIZ LEDEE
CERTIFIED PUBLIC ACCOUNTANT

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

**To the Honorable Mayor and
Members of the Municipal Legislature
Municipality of Santa Isabel, Puerto Rico**

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Municipality of **Santa Isabel**, Puerto Rico (Municipality), as of and for the fiscal year ended June 30, 2012, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated July 10, 2013. The report on the governmental fund financial statements was qualified for the interfund balances. In addition, we did not express an opinion on the governmental wide financial statements because we were unable to obtain sufficient and competent evidential matter related to the capital assets and we were unable to obtain an evaluation of the legal cases from the external lawyers of the Municipality. Except as discussed in the preceding sentence, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses. Findings 12-II-02 and 12-II-03.

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 (CONTINUED)

Internal Control Over Financial Reporting (continued)

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompany Schedule of Findings and Questioned Costs to be significant deficiencies. Finding 12-III-01, 12-II-04, 12-II-05, 12-III-06 and 12-III-07.

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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items 12-II-01, 12-II-02, 12-II-03 and 12-II-07.

We noted certain matters that we reported to management of the Municipality in a separate letter dated July 10, 2013.

The Municipality's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the Municipality's response and, accordingly, we express no opinion on it.

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


Pedro C. Ortiz Ledee, CPA
License Number 5200

Guayama, Puerto Rico
July 10, 2013

Stamp Num. 2671583 was affixed
to the original of this report



PEDRO C. ORTIZ LEDEE
CERTIFIED PUBLIC ACCOUNTANT

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

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**To the Honorable Mayor and
Member of the Municipal Legislature
Municipality of Santa Isabel, Puerto Rico**

Compliance

We have audited Municipality of **Santa Isabel**, Puerto Rico (Municipality) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Municipality's major federal programs for the fiscal year ended June 30, 2012. 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 grants applicable to each of its major federal programs is the responsibility of the Municipality's management. Our responsibility is to express an opinion on Municipality's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about 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 items 12-III-09 and 12-III-12 in the accompanying Schedule of Findings and Questioned Costs, the Municipality did not comply with requirements regarding Cash Management and Reporting that are applicable to its Community Development Block Grant. Compliance with such requirement is necessary, in our opinion, for the Municipality, to comply with the requirements applicable to that program.

As described in item 12-III-13, 12-III-14, 12-III-15, 12-III-16, 12-III-19, 12-III-20 and 12-III-21 in the accompanying Schedule of Findings and Questioned Costs, the Municipality did not comply with requirement regarding Allowable Cost, Allowable Activities, Eligibility, Reporting and Special Tests (findings 12-III-19 through 12-III-21) that are applicable to its Section 8 Housing Choice Voucher. Compliance with such requirement is necessary, in our opinion, for the Municipality to comply with the requirements applicable to that program.

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

Compliance (continued)

As described in items 12-III-23 and 12-III-25 in the accompanying Schedule of Findings and Questioned Costs, the Municipality did not comply with requirements regarding Equipment and Real Property Management and Reporting that are applicable to its Child Care and Development Block Grant. Compliance with such requirement is necessary, in our opinion, for the Municipality, to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the preceding paragraphs, the Municipality complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the fiscal year ended June 30, 2012. The results of our auditing procedures also disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items 12-III-08, 12-III-10, 12-III-11, 12-III-17, 12-III-18, 12-III-22 and 12-III-24.

Internal Control over Compliance

Management of Municipality is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Municipality's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Municipality's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we considered to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 12-III-09, 12-III-12, 12-III-13, 12-III-14, 12-III-15, 12-III-16, 12-III-19, 12-III-20, 12-III-21, 12-III-23 and 12-III-25.

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

Internal Control over Compliance (continued)

A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We considered the deficiencies in internal control over compliance described in the accompanying Schedule of Findings and Questioned costs as items 12-III-08, 12-III-10, 12-III-11, 12-III-17, 12-III-18, 12-III-22 and 12-III-24 to be significant deficiencies.

The Municipality's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the Municipality's responses and, accordingly, we express no opinion on the responses.

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

PE-CATEE!
Pedro C. Ortiz Ledee, CPA
License Number 5200

Guayama, Puerto Rico
July 10, 2013

Stamp Num. 2671584 was affixed
to the original of this report



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

SECTION I – SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Type of auditor’s report issued:	Qualified for fund financial statement and disclaimer of opinion for governmental-wide financial statements	
Internal control over financial reporting:		
Material weakness identified?	Yes X	No
Significant deficiencies identified?	Yes X	No reported
Noncompliance material to financial statements noted?	Yes X	No

Federal awards

Internal Control over major programs:		
Material weakness identified?	Yes X	No
Significant deficiencies identified?	Yes X	No reported
Type of auditor’s report issued on compliance for major programs:	Qualified	
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes X	No

Identification of major programs

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grants/ State’s Program
14.871	Section 8 Housing Choice Voucher
93.575	Child Care and Development Block Grant

Dollar threshold used to distinguish between Type A and Type B programs	\$300,000
Auditee qualified as low-risk auditee?	Yes No X

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-01
REQUIREMENT	ACCOUNTING RECORDS AND REPORTING SYSTEM
CONDITION	The Municipality did not maintain complete and adequate accounting records.
CONTEXT	During our examination of the accounting system, we noted that the Finance Department does not summarize the transactions in a formal general ledger, in order to properly record and account the transactions of the General Fund and the Special Revenue Funds of the Municipality. In addition, the accounting transactions are currently accounted simultaneously through a manual and a computerized accounting system, for which no reconciliation procedures are made among them. These accounting records did not provide for summarization of transactions that permits the preparation of the financial statements in accordance with generally accepted accounting principles of the United States of America (GAAP).
CRITERIA	Article 8.010 (b) of State Act Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991, states that the Municipalities must maintain its fund accounting in accordance with GAAP. In addition, Article 8.010 (c) (1) and (3) states that the system used must produce reliable reports and financial statements, provide complete information about the results of operations and include the necessary internal controls to account for all funds, capital assets and other assets.
CAUSE	The Municipality has not established effective internal control procedures over the accounting records in which the financial transactions of all the funds are recorded.
EFFECT	The Municipality is not in compliance with Articles 8.010 (b) and (c) (1) and (3) of the State Law Number 81 of August 30, 1991.
RECOMMENDATION	We recommend management to establish the necessary internal controls and procedures in order to maintain a complete accounting system which adequately summarizes the accounting information of all the financial transactions related to assets, liabilities, revenues and expenditures of the Municipality's funds. Also, the accounting records of the Municipality should be precisely enough, to support the amounts presented in the financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER 12-II-01 (CONTINUED)

REQUIREMENT ACCOUNTING RECORDS AND REPORTING SYSTEM

**MANAGEMENT RESPONSE AND
CORRECTIVE ACTION PLAN**

The Municipality maintains two set of accounting records; a manual system and a uniform computerized accounting system provided in the past by the Office of the Commissioner of Municipal Affairs (OCAM) to all of the municipalities of Puerto Rico (as required by Law No. 81). The manual system is the primary financial records for financial statements preparation purposes at the end of each fiscal year due to the fact that the computerized system real accounts balances carried forward from prior years were affected by accounting errors in the first years of the system operation.

We are considering alternatives for the acquisition of new accounting software, and therefore, we will hope to solve our accounting system condition in a near future.

Implementation Date: June 30, 2013

Responsible Person: Mrs. Irma M. Vargas
Finance Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-02
REQUIREMENT	ACCOUNTING RECORDS- CAPITAL ASSETS
CONDITION	The Municipality does not have an effective system to account for capital assets, including the infrastructure assets.
CONTEXT	The Municipality does not have a complete and adequate records over the capital assets reported in the governmental activities. Also, the Municipality has not recorded all the infrastructure assets, accordingly, has not recorded depreciation expenses for those assets. These infrastructure assets should be reported as part of the capital assets of the Municipality, according to Statement No. 34 of the Governmental Accounting Standards Board (GASB 34).
CRITERIA	Article 8.010 (c) (3) of the State Law Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico de 1991</i> of August 30, 1991, states that Municipalities should have systems that have effective controls and accounting over the capital assets. Also, GASB Statement No. 34, requires that all capital assets, including infrastructure, must be presented in the Statement of Net Assets and that these assets must be depreciated during its useful life.
CAUSE	The Municipality did not maintain an adequate control of the accountability of its capital assets including the infrastructure.
EFFECT	The Municipality is not in compliance with Article 8.010 (c) (3) of the State Law Number 81 of August 30, 1991. Also, the Municipality is not in compliance with GASB Statement No 34.
RECOMMENDATION	We recommend management and the Property Division of the Municipality to make an inventory of the capital assets, reconcile it with the capital assets subsidiary ledger and document adequately the cost of these assets. In addition, the Municipality should implement adequate internal control procedures to improve the accountability of infrastructure assets.
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	The Municipality's Finance Department staffs continue updating the capital assets subsidiary ledger. In addition, we are considering engaging with a professional to evaluate the Municipality's infrastructure assets.

Implementation Date: June 30, 2014

Responsible Person: Mrs. Irma M. Vargas-Finance Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-03
REQUIREMENT	ACCOUNTING RECORDS- INTERFUND TRANSACTIONS
CONDITION	During the fiscal year 2011-2012, the Municipality transfers special revenue funds to cover operational expenditures.
CONTEXT	During our examination of the accounting records, we noted that the Municipality does not maintain adequate internal controls over the interfund transactions. This situation caused that various special revenue funds were used as loans, to paid operational costs of the General Fund during fiscal year 2011-2012. In addition, the Municipality did not maintain adequate subsidiary records to accurately account for the interfund balances presented in the Balance Sheet, for the fiscal year 2011-2012.
CRITERIA	Article 8.004 (c) of the State Law Number 81 - <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico de 1991</i> - August 30, 1991, states that the restricted funds received by the Municipalities should be only used for the purposes established by these resources. In addition, Article 8.010 (C) (2) and (3) of State Act Number 81- <i>Ley de Municipios Autonomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991, states that Municipalities should maintain adequate and necessary financial information for the Municipalities administration and the accounting system used must provide effective controls and accounting of all the funds.
CAUSE	The Municipality did not maintain adequate internal control of the accountability of the interfund transactions and the due from and due to account balances.
EFFECT	The Municipality is not in compliance with Articles 8.004 (c) and 8.010 (c) (2) and (3) of the State Law Number 81 - <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico de 1991</i> .
RECOMMENDATION	We recommend management to implement procedures in order to obtain and maintain all the required documentation regards the interfund transactions. In addition, the Municipality should avoid any transfer of special revenue funds unless are adequately supported and are for allowable activities approved by the grantors.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-03 (CONTINUED)
REQUIREMENT	ACCOUNTING RECORDS- INTERFUND TRANSACTIONS
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>The Municipality's Finance Department staffs were instructed to maintain a subsidiary ledger of interfund transactions, and to maintain in file the supporting documentation of all the intefund transactions.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mrs. Irma M. Vargas Finance Department Director</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-04
REQUIREMENT	ACCOUNTING RECORDS- BANK RECONCILIATIONS
CONDITION	The Municipality does not have effective internal control procedures to ensure that the bank reconciliations were reconciled with the accounting records.
CONTEXT	<p>During our cash test, we noted that the reconciliation process for the Municipality's cash accounts consists only of including the ending bank balance, less the outstanding checks of the month. Therefore, there was not a monthly reconciliation process with the Model 4A, which is the manual accounting system that summarized the cash transactions of the General Fund and the special revenue funds.</p> <p>In addition, the payroll bank account was not reconciled at June 30, 2012. Also, we noted that the accounting personnel did not prepare a bank reconciliation for the accounts without movement during a month.</p>
CRITERIA	Chapter IV, Section 12 of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM), establishes that the accounting system of the municipalities shall provide for the timely and accurate preparation of bank reconciliations. In addition, the Municipality shall prepare a monthly report of revenues and disbursements, which has to be reconciled with the bank reconciliations.
CAUSE	The Municipality's internal control procedures failed to assure that the bank reconciliations were prepared in a complete manner and reconciled with the accounting records.
EFFECT	The Municipality is not in compliance with Chapter IV, Section 12 of the Municipal Administration Regulatory Manual of the OCAM.
RECOMMENDATION	We recommend management to improve the internal control procedures over the preparation of the bank reconciliations and assure that accounting records are reconciled monthly with the bank reconciliations within a reasonable amount of time in order to maintain proper control over cash.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER 12-II-04 (CONTINUED)

REQUIREMENT ACCOUNTING RECORDS- BANK RECONCILIATIONS

**MANAGEMENT RESPONSE AND
CORRECTIVE ACTION PLAN**

The Municipality's Finance Department staffs were instructed to reconcile the banks accounts with the Model 4-A in a monthly basis. Also, to correct the finding about the payroll bank account and the inactive bank accounts, we instructed the employee with the responsibilities to prepare all (active or inactive) the account bank reconciliations to reconcile these bank accounts in a reasonable lap of time after the end of each month, not to exceed 30 days.

Implementation Date: August 31, 2013

Responsible Person: Mrs. Irma M. Vargas
Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-05
REQUIREMENT	INTERNAL CONTROLS AND PROCEDURES OVER THE REVENUES CYCLE
CONDITION	The Municipality does not have effective internal control procedures to ensure that the revenue transactions are properly and accurately recorded.
CONTEXT	<p>During our cash and revenues test, we noted that, during the fiscal year 2011-2012, the Municipality did not maintain an accounting register for the revenue transactions. In addition, the Municipality did not prepare official receipts to the cash collections for the daily revenues. Also, we noted the following deficiencies over the revenues cycle:</p> <ul style="list-style-type: none">a. We found that the responsible employees were not preparing the cash receipts for the monthly revenues related with the property taxes of the Municipality;b. We noted that the accounting personnel did not maintain an adequate register related to the collections of the volume of business taxes. In addition, these collections were not registered in the Municipality's computerized accounting system.
CRITERIA	Chapter III, Sections 3, 4 and 5 of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM), establishes the procedures and controls that the Municipalities should follow regarding the revenue and collection cycle.
CAUSE	The Municipality is not following the internal control procedures established for the revenues and collections cycle.
EFFECT	The Municipality is not in compliance with Chapter III, Sections 3, 4 and 5 of the Municipal Administration Regulatory Manual of the OCAM.
RECOMMENDATION	We recommend management to establish a manual or electronic accounting register in which the revenues transactions are adequately codified by revenues concepts and by funds. In addition, we recommend that the responsible employees should prepare official receipts to all the revenues received by the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-05 (CONTINUED)
REQUIREMENT	INTERNAL CONTROLS AND PROCEDURES OVER THE REVENUE CYCLE
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We will improve our collections and revenues procedures in order to correct the conditions reported in this finding by the external auditors, providing technical training to the Finance Department Staff and increasing supervision on such procedures. Implementation Date: August 31, 2013 Responsible Person: Mrs. Irma M. Vargas Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-06
REQUIREMENT	INTERNAL CONTROLS AND PROCEDURES OVER THE DISBURSEMENT CYCLE
CONDITION	During the fiscal year 2011-2012, the Municipality disbursed funds without the appropriate supporting documentation.
CONTEXT	<p>During our examination of the Municipality's disbursement process, we examined sixty (60) checks of the General Fund and other special revenue funds (eighty-one (81) disbursement vouchers) and noted the following deficiencies:</p> <ul style="list-style-type: none">a. In thirty-one (31) disbursements vouchers, the invoices, were not marked as paid or cancelled;b. Sixty (60) disbursement vouchers were not approved (signed) by one of the responsible employees;c. In five (5) disbursement vouchers, the purchase orders were not approved (signed) by one of the responsible employees;d. In five (5) disbursement vouchers the original supplier's invoice was not available for our examination. In addition, in one (1) disbursement voucher the original supplier's invoice, did not include the price per article and did not include the total amount to be paid by the Municipality;e. In one (1) disbursement voucher, the receiving report from the supplier was not available for our examination;f. In twenty-eight (28) disbursement vouchers, the purchase orders were issued after the invoices and the services or goods were received;g. In forty-four (44) disbursement vouchers, we noted that the acquisition process (quotations) was not properly documented, or was incomplete.
CRITERIA	The Chapter IV of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affairs (OCAM), establishes the internal control procedures that the Municipalities should follow during the disbursement cycle.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-06 (CONTINUED)
REQUIREMENT	INTERNAL CONTROLS AND PROCEDURES OVER THE DISBURSEMENT CYCLE
CAUSE	The Municipality's internal control failed to assure that the disbursement vouchers contains all the documentation required by Law.
EFFECT	The Municipality is not in compliance with the Chapter IV of the Municipal Administration Regulatory Manual of the Puerto Rico Commissioner's Office for Municipal Affair (OCAM).
RECOMMENDATION	We recommend management to improve the internal control procedures in order to obtain and maintain all the required documentation and supporting documents related to the disbursements process prior to the issuance of the checks.
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We will improve our purchases and expenditures procedures in order to correct the conditions reported in this finding by the external auditors, providing technical training to the Finance Department Staff and increasing supervision on such procedures. Implementation Date: August 31, 2013 Responsible Person: Mrs. Irma M. Vargas Finance Department Director

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	12-II-07
REQUIREMENT	SINGLE AUDIT SUBMISSION
CONDITION	The Municipality did not comply with the required due date for the submission of the Single Audit Report.
CONTEXT	The Municipality did not submit, in a timely manner, the Single Audit Reporting package for the fiscal year ending on June 30, 2012. The due date for this report was no later than March 31, 2013.
CRITERIA	OMB Circular A-133, Subpart C, Section 320 (a) states that all audits shall be completed and submitted to the Federal Audit Clearinghouse and the cognizant agency within the earlier of 30 days after receipt of the auditor's report or nine (9) months after the end of the audit report.
CAUSE	Due to the lack of adequate accounting records, the Municipality did not comply with the requirements established in OMB Circular A-133.
EFFECT	The Municipality is not in compliance with OMB Circular A-133, Subpart C, Section 320 (a). Also, the Municipality could be sanctioned by the Federal Government for the non compliance of this requirement.
RECOMMENDATION	We recommend management to establish adequate accounting records that allow for the timely completion of its financial statements and performance of the Single Audit.
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We gave instruction to the Finance Department to submit, in a timely manner, all the required financial information, to our external auditors, in order to comply with the datelines for the submission of the Single Audit Report for the fiscal year 2012-2013, which is March 31, 2014. Implementation Date: August 31, 2013 Responsible Person: Mrs. Irma M. Vargas Finance Department Director

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-08
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES- HOUSEKEEPING SERVICES
CONDITION	The Program failed to maintained appropriate supporting documentation regarding the housekeeping services participant's files.
CONTEXT	As part of our grant disbursement test, we examined ten (10) housekeepers' files and noted the following conditions: a. No case numbers were assigned to the participant's files; b. In the ten (10) participant's files, we did not found evidence of the monthly follow up visits made by the Program coordinator to the participants.
CRITERIA	The Municipality has an operational guide " <i>Manual Operacional- Programa Auxiliares del Hogar</i> " that includes all procedures and program's requirements for housekeeping services.
CAUSE	The Program's internal controls procedures failed to assure that the required monthly visits and inspections to monitor the services, were realized in accordance to the pass-through operational guides.
EFFECT	The Program is not in compliance with the operational guide related to the housekeeping services.
RECOMMENDATION	We recommend management to implement adequate internal controls and procedures in order to assure that the Program's staff monitors the services in accordance with the regulations and the operational guides.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-08 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES- HOUSEKEEPING SERVICES
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>We are going to instruct the Program's staff with the responsibilities to maintain the housekeeper's files in compliance with the Program regulations and the operational guide provided by the pass-through entity. Also, we will instruct the staff, to follow all the procedures and to use all the forms specified in the operational guide.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-09
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	CASH MANAGEMENT
CONDITION	The Program did not minimize the time between the receiving of the requested funds from the pass-through entity, and the disbursement of these funds.
CONTEXT	During our cash management test, we noted that the Program used two (2) bank accounts for the deposits of the CDBG funds, which maintained a combined average cash balance of approximately \$133,260 during the fiscal year 2011-2012. Also, we examined five (5) requests of funds made by the Program to the pass-through entity, and found that two (2) of these requests took between ten (10) and fifty-three (53) days from the moment the funds were received and the issuance of the checks.
CRITERIA	Code of Federal Regulations 24, Section 570.489 (c) (1) states that units of general local governments shall use procedures to minimize the time elapsing between the transfer of funds by the State and disbursement made by the grantee for CDBG activities.
CAUSE	The Federal Programs and Finance Department of the Municipality did not maintain appropriate cash management procedures in order to request funds to the pass-through agency only for immediate needs.
EFFECT	The Program is not in compliance with Code of Federal Regulations 24, CFR 570.489 (c) (1).
RECOMMENDATION	We recommend management to strengthen its disbursements procedures to minimize the time between the transfer of funds by the pass-through entity and the disbursements made by the Municipality. In addition, the Program should only request funds for immediate needs.
QUESTIONED COSTS	None

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-09 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	CASH MANAGEMENT
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>We will instruct our Program accountant to follow the established procedures to drawdown and disburse the funds, in a timely manner, in order to demonstrate compliance with the cash management regulations.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-10
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	EQUIPMENT AND REAL PROPERTY MANAGEMENT
CONDITION	The Program did not maintain adequate controls over the property and equipment acquired with CDBG Funds.
CONTEXT	<p>During our property and equipment test, we noted that the property register did not include the condition of the property, the ultimate disposition data, nor the date of disposition. Also, we selected a sample of four (4) items from the property register of the Program and noted the following conditions:</p> <ul style="list-style-type: none">a. Two (2) items, that were not in functions, were maintained in the register;b. Two (2) items, which were recorded in the register, were not found physically.
CRITERIA	Code of Federal Regulation 24, Section 85.32 (d) (1) and (2), states that property records must be maintained and it shall includes; (1) a description of the property; (2) serial number or other identification number; (3) the source of property, percentage of Federal participation in the property; (4) the location; (5) use and condition of the property; (6) any ultimate disposition data including the date of disposal; and (7) sale price of property; (8) the acquisition date and the cost of the property. Also, a physical inventory of the property must be taken and the result reconciled with the property records at least on every two years, respectively.
CAUSE	The Program does not have adequate internal control procedures that guarantee adequate records and the safeguarding of the Federal property.
EFFECT	The Program is not in compliance with 24 CFR 85.32 (d) (1) and (2).

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-10 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM; (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	EQUIPMENT AND REAL PROPERTY MANAGEMENT
RECOMMENDATION	The Program should continue updating the property register by including the condition and the date of disposition of the equipment that are being disposed. In addition, a physical inventory should be made to update the property register.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Actually, the Municipality's Finance Department staffs continue updating the capital assets subsidiary ledger in order to comply with the GASB No. 34 capital assets requirements for the fiscal year ended on June 30, 2013. Therefore, we will request to the Property Division staff to take into considerations the requirements established in the Federal regulation. Implementation Date: August 31, 2013 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-11
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS- OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	PROCUREMENT AND SUSPENSION AND DEBARMENT
CONDITION	The Municipality formalized contracts and did not verify if the contractors were suspended or debarred by the Federal government.
CONTEXT	During our suspension and debarment test, we selected a sample of two (2) construction contracts, and we did not found evidence that demonstrated if the Municipality verified the Excluded Parties List System (EPLS) maintained by the General Service Administration, nor obtained a certification from the contractors, to assure that this contractors were not suspended or debarred by the Federal government.
CRITERIA	Code of Federal Regulations 24, Section 85.35 states that grantees and subgrantees must not make any award or permit any award at any tier to any party that is debarred or suspended or is otherwise excluded from or ineligible for participation in federal assistance programs subject to 2 CFR part 2424.
CAUSE	The Program did not maintain appropriate procurement standard procedures to assure that a contract was verify against the EPLS, to assure that the contractors were not suspended or debarred at the moment of the formalization of the contracts.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 85.35.
RECOMMENDATION	We recommend management to obtain the EPLS in printed or electronic format, every time the Municipality formalized a contract in excess of \$25,000 with Programs' funds. Also, the Municipality should verify the contractors against the EPLS list.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-11 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS-THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS- OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	PROCUREMENT AND SUSPENSION AND DEBARMENT
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	To correct this condition, we gave instructions to our Contract Division and the Federal Program Director, to include in our procurement procedures, a step to verify through the electronic version available on the Internet whether or not the individual or entity, are on the list of excluded parties. Implementation Date: August 31, 2013 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-12
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
CONDITION	The Program did not maintain accurate accounting records of the financial transactions, and did not reconcile monthly, the cash account with the bank reconciliations.
CONTEXT	During our reporting test, we noted that the Program did not maintain adequate accounting records, and did not summarize the information of all the financial transactions, related to assets, liabilities, revenues and expenditures of the Program, in a formal general ledger. Also, we found that the accumulative expenditures reported in the quarterly reports of the fiscal year 2011-2012, submitted to the pass-through entity (OCAM), did not reconcile with the accounting records (check register) for the amount of \$24,623. In addition, the cash balance at June 30, 2012, reported in the quarterly reports, does not agree with the bank reconciliation for the amount of \$158,542.
CRITERIA	Code of Federal Regulations 24, Section 85.20 (b) (1) states 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. Code of Federal Regulations 24, Section 85.20 (b) (2) requires that grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially- assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, and income.
CAUSE	The Program failed to establish adequate internal controls over the accounting records. Also, the Program is not reconciling its accounting records with the quarterly reports in order to assure that there are no differences. In addition, the Program is not reconciling on a monthly basis the accounting records with the bank reconciliations.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-12 (CONTINUED)
FEDERAL PROGRAM	COMMUNITY DEVELOPMENT BLOCK GRANTS / STATE'S PROGRAM (CFDA NO. 14.228) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT PASS THROUGH STATE – OFFICE OF COMMISSIONER OF MUNICIPAL AFFAIRS - OCAM
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
EFFECT	The Program did not submit accurate quarterly reports to the pass-through entity in order to comply with the pass-through agency requirements and the Federal regulation.
RECOMMENDATION	The Program should implement adequate accounting records to ensure that financial information submitted to the pass-through entity in its monthly reports agrees with the accounting records.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>In order to maintain adequate and accurate accounting records for the CDBG Program transactions; we gave instruction to the Federal Program department to improve the actual set of manual accounting records. Also, the Program accountant was instructed to reconcile on a monthly basis the accounting records and the bank reconciliation and to assure that the quarterly reports are supported and easily traceable to the accounting records.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

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**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-13
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE COST
CONDITION	During the fiscal year 2011-2012, the Program disbursed funds for activities not related to HAP and administrative fees.
CONTEXT	<p>During our audit, we noted that the Municipality's Internal Audit Department issues a report dated September 20, 2011, where it mentioned various findings related to the disbursements of the Section 8 funds. In this report, allegedly, the Program Coordinator made disbursement transactions in an irregular manner. To validate this information, we selected a sample of seven (7) checks totaling \$4,190, issued by the Program during the months of July, August and September 2011, and noted the following conditions:</p> <ul style="list-style-type: none">a. These checks were issued to one (1) person, and we did not find evidence to corroborate if this person was owner or participant of the Program during the fiscal year 2011-2012;b. Five (5) checks were endorsed (signed) by the person to whom were issued the checks, and apparently, by the Program Coordinator. <p>These checks were evaluated by the Municipality's Internal Audit Department as part of their monitoring procedures, and were included as findings in the report issued by this Department in September 20, 2011.</p>
CRITERIA	Code of Federal Regulation 24, Section 982.157 (b) states that Program receipts must be used in accordance with the PHA's HUD approved budget. Such Program receipts may only be used for: (1) housing assistance payments; and (2) PHA administrative fees.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-13 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE COST
CAUSE	The Program has not properly maintained adequate internal controls over the documents that justify the disbursements. In addition, the lack of an adequate HAP register in which the amounts paid monthly to the owners and participants should be properly recorded and maintained. Also the Program did not maintain an adequate segregation of duties.
EFFECT	The lack of internal controls in the disbursement process and the inadequate segregation of duties, lead the Program to make unsupported payments during the fiscal year 2011-2012.
RECOMMENDATION	We recommend management to continue strengthening the internal controls and procedures designed in the Municipality, to appropriately review the payments vouchers and all the supporting documentation prior to the issuance of a payment.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	The mentioned condition was responsibly reported to the Puerto Rico Department of Justice, Puerto Rico Office of the Comptroller, and the US Department of Housing and Urban Development – Caribbean Office. Also we will take administrative measures in order to reorganize the Program operations to avoid the occurrence of a similar situation in the future, considering the attainment of an adequate segregation of duties. Implementation Date: August 31, 2013 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-14
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES
CONDITION	Program personnel with inadequate segregation of duties.
CONTEXT	During our examination, we noted that the Program maintained two (2) employees during fiscal year 2011-2012. Those employees performs the following tasks and procedures without adequate supervision: (1) maintain and update the waiting list; (2) obtain documentation from applicants and participants and perform the annual reexaminations; (3) completes and submits the Family Report (HUD-50058) and determined the HAP and negative rents; (4) prepare the participants and owner contracts and prepare the purchase orders and disbursement vouchers for payment; (5) maintain custody of the participants files and other documentation; (6) register transactions in the accounting records; and (7) perform the HQS inspections.
CRITERIA	Code of Federal Regulation 24, Section 85.20 (b) (3) states that effective control and accountability must be maintained 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.
CAUSE	The Program failed to establish adequate segregation of duties over the performance, review and recordkeeping of the program tasks in order to comply with Federal regulations.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 85.20 (b) (3).
RECOMMENDATION	We recommend management assignment of additional personnel including a supervisor, to monitor the daily activities of the Program. Also, the Municipality should promote technical training among the assigned employees in the specific areas of the Program.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-14 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ALLOWABLE ACTIVITIES
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>We are taking the administrative measures in order to reorganize the Program operations to avoid the occurrence of a similar situation in the future, considering the attainment of an adequate segregation of duties. Actually, we appointed a Program Coordinator that is supervised by the Program Director, and the accounting transactions are being processed by a Program Accountant with the support of the Municipality's Finance Department Staff.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-15
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELIGIBILITY
CONDITION	The Program failed to document properly the eligibility process.
CONTEXT	<p>During our eligibility test, we examined fifteen (15) participant's files, and we noted the following conditions:</p> <ul style="list-style-type: none">a. In two (2) participant's files, the Enterprise Income Verification (EIV) was not available for examination. In addition, we noted that verifications made in the EIV system for three (3) participant's files reflected incomes that were not considered in their respective HAP calculation. We did not found evidence of the follow-up made by the Program to validate those incomes;b. In three (3) participant's files, we noted that other members of the family did not signed the release forms that allow the Program to obtain information from third parties and employment verification (Privacy Act Notice). In addition, we did not found evidence in four (4) participant's files of the date in which the Privacy Act Notices were signed by the head of households and other members;c. In three (3) participants files, the incomes reported in the Form HUD-50058, did not agree with third party income verification. Also, for three (3) participants, the family members included in the Form HUD-50058 did not agree with the third party income verification;d. In one (1) participant file, we noted that the Program calculated the income in a monthly basis instead of a biweekly basis. This situation caused that the Program reported \$580 annually less in the HAP calculation of this participant;e. In one (1) participant file, we found that the third party evidence was a copy, and the section that includes the income information was erased.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-15 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELIGIBILITY
CRITERIA	<p>Code of Federal Regulation 24, Section 982.516 (a) (1) states that the PHA must conduct a reexamination of family income and composition at least annually; (2) the PHA must obtain and document in the tenant file third party verification of the following factors or must document in the 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 affects the determination of adjusted income.</p> <p>In addition, Code of Federal Regulation, 24, Section 982.516 (g), states that as a condition of admission to or continued assistance under the program, 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. In addition, Chapter G of the Municipality's Administrative Plan establishes the policies and procedures for third parties verifications.</p>
CAUSE	<p>The Program failed to maintain adequate internal controls that assure that annual reexaminations were calculated using the information obtain from third parties. Also, the Program has not established adequate internal controls over the use of the EIV System during the mandatory annual and interim reexamination as a third party income verification of the family income.</p>
EFFECT	<p>The Program is not in compliance with Code of Federal Regulation 24, Section 982.516 (a) (1), (2) and (g) and the Administrative Plan.</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-15 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELIGIBILITY
RECOMMENDATION	We recommend management that the HAP calculations made during the annual reexaminations are prepared using the third parties verifications. We also recommend strengthening the internal controls and procedures designed to verify the family income and composition using the EIV system in each mandatory reexamination of the participants.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>The new Program Coordinator have been instructed to ensure that annual reexaminations were calculated using the information obtain from third parties, and about the requirement to the use of the EIV System during the mandatory annual and interim reexamination as a third party income verification of the family income.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-16
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
CONDITION	The Program did not maintain accurate accounting records of the financial transactions.
CONTEXT	<p>During our reporting test, we noted that the Program did not maintain adequate accounting records, and did not summarize the information of all the financial transactions, related to assets, liabilities, revenues and expenditures of the Program, in a formal general ledger. Also, we found that the accumulative expenditures reported monthly in the Voucher Management System (VMS), are not traceable to the accounting records of the Program.</p> <p>In addition, the Municipality failed to submit, in a timely manner, the audited financial information for the fiscal year 2011-2012 to HUD, through the FASS-PH system.</p>
CRITERIA	Code of Federal Regulations 24, Section 982.158 (a) states that the PHA must 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. The records must be in the form required by HUD, including requirements governing computerized or electronic forms of record-keeping. The PHA must comply with the financial reporting requirements in 24 CFR part 5 Subpart H. In addition, CFR 24, Section 5.801 (b) (1) states that submission of financial information must be prepared in accordance with Generally Accepted Accounting Principles; (2) submitted electronically to HUD through the internet, or in such other electronic format designated by HUD, or in such non-electronic format as HUD may allow if the burden or cost of electronic reporting is determined by HUD to be excessive.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-16 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
CAUSE	The Program failed to establish adequate internal controls over the accounting records and is not reconciling its accounting records with the monthly reports in order to assure that there are no differences. In addition, the Program is not complying with the due dates established by HUD to submit the audited reports.
EFFECT	The Program did not submit to HUD, the required reports, in a timely manner and adequately supported, in order to comply with the Federal regulation.
RECOMMENDATION	The Program should implement adequate accounting records to ensure that the financial information submitted to HUD in its monthly reports agrees with the accounting records and are properly supported.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>In order to maintain adequate and proper accounting records for the Section 8 Housing Choice Voucher transactions; we will improve our set of manual accounting records. Also, we will submit, in a timely manner, the audited information of the Program, for the fiscal year 2012-2013, through the FASS-PH system.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-17
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- REASONABLE RENT
CONDITION	The determination of the reasonable rent to owners was not properly documented by the Program.
CONTEXT	During our reasonable rent test, we examined a sample of fifteen (15) participant's file and found the following conditions: a. In one (1) participant's file, we did not found the reasonable rent study for a change of unit made during the fiscal year 2011-2012; b. In one (1) participant's file, for another change of unit, we did not found the date in which the reasonable rent study was made; c. In one (1) participant's file, we did not found evidence that demonstrated that a reasonable rent study was made that justify such increase in rent.
CRITERIA	Code of Federal Regulation 24, 982.507 (a) (1) states that the PHA may not approve a lease until the PHA determines that the initial rent to owner is a reasonable rent; (2) the PHA must redetermine the reasonable rent: (a) before any increase in the rent to owner; (b) if there is a five percent decrease in the published FMR in effect 60 days before the contract anniversary as compared with the FMR in effect one year before the contract anniversary; and (c) if directed by HUD.
CAUSE	The Program did not maintain adequate documentation in the participant files to support the basis for the determination that the rent paid to the owners are reasonable.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 982.507 (a) (1) and (2).

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-17 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- REASONABLE RENT
RECOMMENDATION	We recommend management to strengthen the internal control procedures to assure that the rents paid to the owners are reasonable. Also, we recommend that adequate and proper documentation about the reasonable rent determination is maintained in the participant's files.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>The new Program Coordinator engaged to administrate the programmatic activities was instructed to ensure the properly documentation and approval of reasonable rent determination when required.</p> <p>Implementation Date: August 31, 2013</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-18
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- HOUSING QUALITY STANDARDS INSPECTIONS/ HQS ENFORCEMENT
CONDITION	The Program failed to document properly the housing quality inspections during the fiscal year 2011-2012.
CONTEXT	<p>During our test, we examined fifteen (15) participant's files, in order to verify if the Program follows the Housing Quality Standards, and noted the following conditions:</p> <ul style="list-style-type: none">a. In one (1) participant file, we noted that the inspector that made the housing quality standard did not documented adequately if the inspection was passed, failed or inconclusive;b. In two (2) participant's files, in which the inspections made were "failed", we did not found evidence that the required corrections were made within thirty (30) calendar days of the inspections.
CRITERIA	Code of Federal Regulations 24, Subpart D, Section 982.158 (a) states that the PHA must maintain complete and accurate accounts and other records for the program in accordance with HUD requirements. Also CRF 982.158 (d) states that the PHA must prepare a unit inspection report.
CAUSE	The Program failed to properly document the corrections of deficiencies made by the owners within the time frame specified by the Federal regulation.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 982.158 (a) and (d).
RECOMMENDATION	We recommend management to continue strengthening internal control procedures to document adequately the correction time period to assure that the units Housing Quality Standards deficiencies were corrected during the specified period established by the Federal regulation.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-18 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- HOUSING QUALITY STANDARDS INSPECTIONS/ HQS ENFORCEMENT
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We gave instructions to the employee responsible of the HQS of the Program to ensure that the annual inspection and the corrections made by the owners or the participants to the units are properly documented in the files. Implementation Date: August 31, 2013 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-19
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- HOUSING ASSISTANCE PAYMENT (HAP)
CONDITION	The Program did not maintain an updated HAP register. Also, there were differences between the amount of HAP reported in the HUD-50058 and the payments made to the owners and participants.
CONTEXT	<p>As part of our housing assistance payment (HAP) test, we found that the Program did not maintain an updated HAP register for the fiscal year 2011-2012.</p> <p>In addition, we selected a sample of fifteen (15) participant's files, and noted that for two (2) HAP payments to owners, the checks paid for the month of June 2012 did not agree with the amounts reported in the HUD-50058. Also, we noted that the Program did not paid \$4.00 of negative rent to a participant applicable to the month of June 2012.</p>
CRITERIA	Code of Federal Regulations 24, Section 982.158 (a) states that the PHA must 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. The records must be in the form required by HUD, including requirements governing computerized or electronic forms of record-keeping. The PHA must comply with the financial reporting requirements in 24 CFR part 5 Subpart H.
CAUSE	The Program controls and procedures failed to assure that all HAP transactions are being recorded in a HAP register. Also, the Program failed to assure that the payments made to the owners and participants were in accordance with the HAP determination in the HUD-50058.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 982.158 (a).

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-19 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- HOUSING ASSISTANCE PAYMENT (HAP)
RECOMMENDATION	We recommended management to prepare a HAP register in order to include all the necessary information related to the HAP payments. This register could be prepared in an electronic worksheet.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Actually, we are preparing a HAP Register, which includes all the required information, in an electronic worksheet. This worksheet will include the minimum requirements of content. Implementation Date: August 31, 2013 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-20
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- ROLLING FORWARD EQUITY BALANCES
CONDITION	The Program did not maintain complete and accurate accounts over the roll-forward equity balances.
CONTEXT	During our examination of the accounting records, we noted that the Program did not maintain adequate records and a proper accounting of the roll-forward balances of the administrative fee and HAP equities. In addition, the amounts of equity reported in the Voucher Management System (VMS) during the fiscal year 2011-2012 were not traceable to the accounting records, and were not properly supported with adequate documentation.
CRITERIA	Code of Federal Regulations, 24 CFR, Section 982.158 (a) (b) states that the PHA must 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. The records must be in the form required by HUD, including requirements governing computerized or electronic forms of record-keeping. Also, the PHA must furnish to HUD accounts and other records, reports, documents and information, as required by HUD.
CAUSE	The Program has not established accounting procedures to ensure that the HAP and administrative fee equity accounts are properly accounted and supported with adequate documentation.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 982.158 (a) (b).
RECOMMENDATION	We recommended management to prepare an analysis of the accounting of the HAP and the administrative fee equity accounts since year 2004 and adjust or correct any errors that affects these equity balances.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-20 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- ROLLING FORWARD EQUITY BALANCES
QUESTIONED COSTS	None

**MANAGEMENT RESPONSE AND
CORRECTIVE ACTION PLAN**

To correct the condition reported by the external auditors, we will modify the existing records in order to assure that the accounting records reflects the financial position and the results of operation, in sufficient detail to permit an easily audit trial and preparation on time of required financial reports. Also, we will prepare an analysis of the Administrative and HAP equities and made the necessary adjustments to reflect the corrected balances at June 30, 2013.

Implementation Date: September 30, 2013

Responsible Person: Mr. Ricardo Burgos Colón
Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-21
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- DEPOSITORY AGREEMENTS
CONDITION	The Municipality failed to enter in a depository agreement with its financial institution.
CONTEXT	During our evaluation, we did not identify evidence of a depository agreement in the form required by HUD with the depository institution of the Municipality.
CRITERIA	Code of Federal Regulation 24, Section 982.156 (a) states that unless otherwise required or permitted by HUD, all program receipts must be promptly deposited with a financial institution selected as depository by the PHA in accordance with HUD requirements. In addition, Code of Federal Regulations 24, 982.156 (c) states that the PHA must enter into an agreement with depository in the form required by HUD.
CAUSE	The Municipality's management failed to enter into an agreement in the form required by HUD with its financial institution.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Subpart D, Section 982.156 (a) and (c).
RECOMMENDATION	We recommend management to contact its financial institution and formalize, as soon as possible, the depository agreement in the form established by HUD.
QUESTIONED COSTS	None

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-21 (CONTINUED)
FEDERAL PROGRAM	SECTION 8 HOUSING CHOICE VOUCHERS PROGRAM (CFDA 14.871) U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	SPECIAL TEST- DEPOSITORY AGREEMENTS
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We are in the process to enter into a depository agreement, in the form required by HUD, with the financial institution in where Program's funds are deposited. Implementation Date: August 31, 2013 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-22
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELIGIBILITY
CONDITION	The Program failed to document properly and in a timely manner, the annual reexaminations of two (2) participants.
CONTEXT	<p>During our eligibility test, we selected a sample of thirty (30) participant's files and found the following condition:</p> <p>a. The Program selected four (4) children using as criteria that the families were searching a job. According with the eligibility criteria established by the pass-through entity, the families has one year to find a job. During our examination we noted that the Program made the annual reexaminations for two (2) of these participants, approximately two months after the end of the year.</p>
CRITERIA	<p>Code of Federal Regulation 45, Section 98.20 (a) states that in order to be eligible for services, a child shall: be under 13 years or up to age 19, if incapable of self care or under court supervision; resides with a family whose income does not exceed 85 percent of the State's median income for a family of the same size; resides with parents who are working or attending a job training or educational program; and receive or need to receive, protective services.</p> <p>Also, Chapter III (4), of the Eligibility Criteria Revision, with effective date of June 1, 2011, of the pass-through entity, states that searching a job consists in the searching of a job for a period of one year, maximum, from the date in which the participant solicited the Program services or was unemployed during the eligibility period. If the participant did not found a job during the one year period, the case will be reevaluated and if did not complied with the established eligibility criteria, the participant can lose the eligibility in the Program.</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-22 (CONTINUED)
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	ELIGIBILITY
CAUSE	The Program failed to assure that annual reexaminations for the eligibility process were made in a timely manner for families which were searching a job.
EFFECT	The Program is not in compliance with Code of Federal Regulation 45, Section 98.20 (a). Also, the Program is not in compliance with the Eligibility Criteria Revision, of the pass-through entity, Chapter III (4).
RECOMMENDATION	We recommend management to continue strengthening the internal control procedures over the annual reexaminations and to continue documenting adequately the eligibility process.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We gave instructions to the Program Coordinator, to ensure that the annual reexaminations of the participants are made, in a timely manner and with adequate third party income verifications. Implementation Date: August 31, 2013 Responsible Person: Mrs. Willdemary Vázquez Rodríguez Federal Programs Director

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-23
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	EQUIPMENT AND REAL PROPERTY MANAGEMENT
CONDITION	The Program did not maintain adequate controls over the property and equipment, acquired with Child Care and Development Block Grant funds.
CONTEXT	During our equipment and real property management test, the Program could not provide us a property ledger, updated at June 30, 2012, which includes all the necessary information related to the Program’s assets.
CRITERIA	Code of Federal Regulation 45 part 92.32 (d) (1), states that property records must be maintained and it shall includes; (1) a description of the property, (2) serial number or other identification number; (3) the source of property, (4) who holds title, (5) the acquisition date (6) cost of the property, (7) percentage of Federal participation in the property, (8) the location, (9) use and condition of the property, and (10) any ultimate disposition data including the date of disposal. Also, a physical inventory of the property must be taken and the result reconciled with the property records at least on every two years, respectively.
CAUSE	The Program does not have adequate internal control procedures that guarantee adequate records and the safeguarding of the Federal property.
EFFECT	The Program is not in compliance with CFR 45 part 93.32 (d) (1).
RECOMMENDATION	The Program should prepare a property register which includes all the requirements established by the Federal regulation including the date of acquisition and cost. In addition, a physical inventory should be made to reconcile the property register.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-23 (CONTINUED)
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	EQUIPMENT AND REAL PROPERTY MANAGEMENT
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>During the fiscal year 2012-2013, we made a physical inventory of the Program's property. Also, we prepared a subsidiary which includes all the property and equipment acquired with the funds delegated, to the Municipality.</p> <p>Implementation Date: Not applicable</p> <p>Responsible Person: Mrs. Ruby J. Giraldo Meléndez Program Accountant</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-24
FEDERAL PROGRAMS	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	PROGRAM INCOME
CONDITION	The Program did not comply with the program income requirement.
CONTEXT	During our program income test, we noted that the transactions of the Child Care and Development Block Grant's program income were not properly recorded in the accounting records. Also, the Program did not maintain adequate controls over the billing, receipts and deposits of the parents' contributions for the Child Care services.
CRITERIA	Code of Federal Regulations 45, Part 92.25 (a), states that grantees are encouraged to earn income to defray program costs. In addition, CFR 45, Part 92.25 (b) states that program income means gross income received by the grantee or subgrantee directly generated by a grant supported activity, or earned only as a result of the grant agreement during the grant period. Also, the part 12 of the Contract with the pass-through agency (ACUDEN) states that the Municipality is compromised to comply with the procedures established to determine the use of the parents' contributions according to the Federal regulations.
CAUSE	The Program does not maintained appropriate accounting records over the program income transactions.
EFFECT	The Program is not in compliance with Code of Federal Regulations 45, Part 92.25 (a), (b) and part 12 of the Contract with the pass-through entity.
RECOMMENDATION	We recommend management to implement adequate procedures to ensure that the financial transactions related to the program income are properly recorded in the accounting records of the Program.
QUESTIONED COSTS	None

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING	12-III-24 (CONTINUED)
FEDERAL PROGRAMS	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	PROGRAM INCOME
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>To correct the condition reported by the external auditors we will prepare a subsidiary ledger related to the parents' contributions, in which the daily transactions will be properly recorded. Also, the Program's Staff will be properly advised about the requirements to adequately document the parents' contributions transactions related to the Child Care services.</p> <p>Implementation Date: October 1, 2013</p> <p>Responsible Person: Mrs. Ruby J. Giraldo Meléndez Program Accountant</p>

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-25
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
CONDITION	The Program did not maintain accurate accounting records of the financial transactions.
CONTEXT	During our reporting test, we noted that the Program did not maintain adequate accounting records, and did not summarize the information of all the financial transactions, related to assets, liabilities, revenues and expenditures of the programs, in a formal general ledger. Also, we noted that the amounts reported in the quarterly reports during the fiscal year 2011-2012 were not supported by accurate accounting information.
CRITERIA	Code of Federal Regulations 45, 92.20 (b) (2), states that grantees and subgrantees must maintain records which adequately identify the source and application of funds provided for financially-assisted activities. These records must contain information pertaining to grant or subgrant awards and authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures and income.
CAUSE	The Program failed to establish adequate internal controls over the accounting records and is not reconciling its accounting records with the quarterly reports in order to assure that there are no differences.
EFFECT	The Program did not submit accurate quarterly reports that are supported with adequate accounting records to the pass-through entity in order to comply with the Federal regulation.
RECOMMENDATION	The Program should implement adequate accounting records to ensure that financial information submitted to the pass-through entity in its quarterly reports agrees with the accounting records and are adequately supported.

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**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	12-III-25 (CONTINUED)
FEDERAL PROGRAM	CHILD CARE AND DEVELOPMENT BLOCK GRANT – (CFDA 93.575) U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES PASS THROUGH STATE – ADMINISTRATION OF CHILDREN AND FAMILIES
REQUIREMENT	COMPLIANCE AND INTERNAL CONTROL
NONCOMPLIANCE	REPORTING
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>To correct the condition reported by the external auditors we will modify the existing records in order to assure that the accounting records present the financial position and the results of operation in sufficient detail to permit an easily audit trial and preparation on time of required financial reports.</p> <p>Implementation Date: October 1, 2013</p> <p>Responsible Person: Mrs. Ruby J. Giraldo Meléndez Program Accountant</p>

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**SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-06	Allowable Cost- Internal controls over the disbursement process	14.228	None	Full corrective action was taken. We improved our internal control procedures over the disbursement process.
11-III-07	Allowable Activities- Housekeeping Services	14.228	None	No corrective action has been taken. Finding Reference 12-III-08.
11-III-08	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-09.
11-III-09	Davis- Bacon Act	14.228	None	Full corrective action was taken. We corrected the deficiencies over the Davis- Bacon Act requirements.
11-III-10	Equipment and Real Property Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-10.
11-III-11	Reporting	14.228	None	No corrective action has been taken. Finding Reference 12-III-12.
11-III-12	Allowable Cost- Disbursement Process	14.871	\$10,380	No corrective action has been taken. Finding Reference 12-III-13.
11-III-13	Allowable Activities- Segregation of Duties	14.871	None	No corrective action has been taken. Finding Reference 12-III-14.
11-III-14	Eligibility	14.871	None	No corrective action has been taken. Finding Reference 12-III-15.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-15	Reporting	14.871	None	No corrective action has been taken. Finding Reference 12-III-16.
11-III-16	Special Test-Waiting List	14.871	None	Full corrective action was taken. We corrected the deficiencies related to the waiting list.
11-III-17	Special Test-Reasonable Rent	14.871	None	No corrective action has been taken. Finding Reference 12-III-17.
11-III-18	Special Test-Utility Allowance Schedule	14.871	None	Full corrective action was taken. We prepared the utility allowance schedule for the fiscal year 2011-2012.
11-III-19	Special Test-Housing Assistance Payment Register	14.871	None	No corrective action has been taken. Finding Reference 12-III-19.
11-III-20	Special Test-Rolling Forward Equity Balances	14.871	None	No corrective action has been taken. Finding Reference 12-III-20.
11-III-21	Special Test-Depository Agreement	14.871	None	No corrective action has been taken. Finding Reference 12-III-21.
11-III-22	Equipment and Real Property Management	93.575	None	No corrective action has been taken. Finding Reference 12-III-23.
11-III-23	Program Income	93.575	None	No corrective action has been taken. Finding Reference 12-III-24.
11-III-24	Reporting	93.575	None	No corrective action has been taken. Finding Reference 12-III-25.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-25	Procurement, Suspension and Debarment	93.713	None	No corrective action has been taken. The auditors did not identified during fiscal year 2011-2012 transactions related to this finding.
10-06	Reporting- Fiscal Requirements	14.228	None	No corrective action has been taken. Finding Reference 12-III-12.
10-07	Reporting	14.228	None	No corrective action has been taken. Finding Reference 12-III-12.
10-08	Equipment and Real Property Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-10.
10-09	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-09.
10-10	Davis- Bacon Act	14.228	None	Full corrective action was taken. We corrected the deficiencies over the Davis- Bacon Act requirements.
10-11	Special Test- Housekeepers Project	14.228	None	No corrective action has been taken. Finding Reference 12-III-08.
10-12	Reporting- Fiscal Requirements	14.871	None	No corrective action has been taken. Finding Reference 12-III-16.
10-13	Activities Allowed- Segregation of Duties	14.871	None	No corrective action has been taken. Finding Reference 12-III-14.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
10-15	Eligibility	14.871	None	No corrective action has been taken. Finding Reference 12-III-15.
10-16	Special Test- Housing Assistance Payment	14.871	None	No corrective action has been taken. Finding Reference 12-III-19.
10-17	Special Test- Waiting List	14.871	None	Full corrective action was taken. We corrected the deficiencies related to the waiting list.
10-18	Special Test- Depository Agreement	14.871	None	No corrective action has been taken. Finding Reference 12-III-21.
10-19	Reporting- Fiscal Requirements	93.575	None	No corrective action has been taken. Finding Reference 12-III-25.
10-20	Program Income	93.575	None	No corrective action has been taken. Finding Reference 12-III-24.
10-21	Equipment and Real Property Management	93.575	None	No corrective action has been taken. Finding Reference 12-III-23.
09-04	Reporting	14.228	None	No corrective action has been taken. Finding Reference 12-III-12.
09-05	Equipment and Real Property Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-10.
09-06	Reporting- Fiscal Requirements	14.228	None	No corrective action has been taken. Finding Reference 12-III-12.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL**

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
09-08	Reporting- Fiscal Requirements	14.871	None	No corrective action has been taken. Finding Reference 12-III-16.
09-09	Reporting- Fiscal Requirements	93.575	None	No corrective action has been taken. Finding Reference 12-III-25.
09-10	Program Income	93.575	None	No corrective action has been taken. Finding Reference 12-III-24.
09-11	Equipment and Real Property Management	93.575	None	Partially corrective action has been taken. Finding Reference 12-III-23.
08-04	Equipment and Real Property Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-10.
08-08	Reporting	93.575	None	No corrective action has been taken. Finding Reference 12-III-25.
08-09	Program Income	93.575	None	No corrective action has been taken. Finding Reference 12-III-24.
08-10	Equipment and Real Property Management	93.575	None	No corrective action has been taken. Finding Reference 12-III-23.
07-06	Equipment and Real Property Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-10.
06-06	Equipment and Real Property Management	14.228	None	No corrective action has been taken. Finding Reference 12-III-10.