

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

**MUNICIPIO DE SANTA ISABEL
AUDITORÍA 2012-2013
30 DE JUNIO DE 2013**

COMMONWEALTH OF PUERTO RICO MUNICIPALITY OF SANTA ISABEL



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SINGLE AUDIT REPORT

For the Fiscal Year Ended June 30, 2013
(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, 2013

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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**

Report on the Financial Statements

I have audited the accompanying financial statements of 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, 2013, and the related notes to the financial statements. I was engaged to audit the financial statements of the governmental activities. These financial statements collectively comprise the Municipality's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

My responsibility is to express opinions on these financial statements based on my audit. I conducted my 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 I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. Because of the matter described in the "Basis for Disclaimer of Opinion on Governmental Activities" paragraph, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the governmental activities.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risk of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, I express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinions.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

Basis for Disclaimer of Opinion on Governmental Activities

The Municipality did not maintain a complete, updated and accurate capital assets subsidiary ledger, in order to obtain sufficient and competent evidential matter related to the capital assets reported in the accompanying statement of net position for \$22,413,405, net of accumulated depreciation of \$9,789,529. The Municipality's records do not permit the application of other auditing procedures to the capital assets.

Disclaimer of Opinion

Because of the significance of the matter described in the "Basis for Disclaimer of Opinion on Governmental Activities" paragraph, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the governmental activities. Accordingly, I do not express, an opinion on the financial position of the governmental activities of the Municipality at June 30, 2013, or the changes in financial position, thereof for the year then ended.

Basis for Qualified Opinion on the General Fund, the State Legislative Joint Resolutions Fund and the aggregate remaining fund

The Municipality did not maintain adequate accounting records of the interfund cash transactions and the corresponding due from and due to account balances. I was unable to obtain sufficient evidence to support and satisfy myself about the amounts recorded in the interfund balances recorded in the General Fund, the State Legislative Joint Resolutions Fund and the aggregate remaining fund in the balance sheet.

Qualified Opinion

In my opinion, except for the possible effects of the matters discussed in the "Basis for Qualified Opinion on the General Fund, the State Legislative Joint Resolutions Fund and the aggregate remaining fund" paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the General Fund, the State Legislative Joint Resolutions Fund and the aggregate remaining fund of the Municipality, as of June 30, 2013, and the respective changes in financial position thereof for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Unmodified Opinions

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Capital Improvement Bonds Fund and the Debt Service Fund as of June 30, 2013, and the respective changes in financial position thereof for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 13 to the financial statements, in 2011, the Municipality entered an Administrative Order on Consent (Docket No. RCRA-02-2011-7303) with the United States Environmental Protection Agency (EPA). The Municipality shall perform the actions required by this Order and comply with its provisions, which includes the permanent closure of the entire landfill no later than December 31, 2013. The Municipality have an obligation under this Order on Consent to comply with any requirement, term, or condition, set forth in or required by this Order, and is subject to penalties for failure to comply. My opinion is not modified with respect to this matter.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

As discussed in Note 1 (s) to the financial statements, during the fiscal year the Municipality adopted new accounting guidance, Governmental Accounting Standards Board (GASB) Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. My opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 5 through 17 and 75 through 77 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. I 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 my inquiries, the basic financial statements, and other knowledge I obtained during my audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

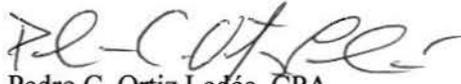
Other Information

My audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Municipality's basic financial statements. The 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. Because of the significance of the matter described in the "Basis for Disclaimer of Opinion on Governmental Activities" paragraph, it is inappropriate to and I do not express an opinion on the supplementary information referred to above.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, I have also issued my report dated November 16, 2014, on my consideration of the Municipality's internal control over financial reporting and on my 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 my 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* in considering Municipality's internal control over financial reporting and compliance.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)



Pedro C. Ortiz Ledée, CPA
License Number 5200

Guayama, Puerto Rico
November 16, 2014

Stamp O2698691 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, 2013

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, 2013. 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, 2012. 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 2012-2013 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 \$31,922,520 at June 30, 2013, of which \$22,413,405 consist of capital assets (net of accumulated depreciation and amortization of \$9,789,529), \$930,882 consist of cash and cash equivalents, \$7,306,888 consist of cash with fiscal agent (which are restricted principally for capital projects and debt service) and \$1,271,345 consist of accounts receivable.
- The Municipality's total liabilities amounted to \$35,321,844 at June 30, 2013, of which \$24,432,500 consist of bonds and notes payable, \$1,406,064 consist of accounts payable and accrued liabilities, \$1,612,019 consist of intergovernmental payables, \$1,588,472 consist of accrued compensated absences, \$1,404,012 consist of unearned revenues, \$215,922 consist of accrued christmas bonus, \$445,797 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 (\$3,399,324) at June 30, 2013.
- The Municipality's total revenues amounted to \$19,515,431 for the fiscal year ended June 30, 2013, of which \$8,110,192 arose from taxes, \$8,556,650 arose from intergovernmental grants and contributions, and \$2,848,589 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, 2013

- The Municipality's total expenses amounted to \$20,300,845 for the fiscal year ended June 30, 2013, of which \$12,695,062 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 \$903,980 of its total expenses, in interests related to its long-term obligations, and \$6,701,803 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, 2013.
- The Municipality's total net position decreased by \$785,414 during the fiscal year ended June 30, 2013.

Governmental Funds' Highlights:

- The total fund balances of governmental funds amounted to \$3,534,294 at June 30, 2013, which are restricted for capital projects, debt service and other specific purposes.
- The governmental funds presented an unassigned fund deficit of (\$5,084,702).
- The fund balances of governmental funds increased by \$754,389 during the fiscal year ended June 30, 2013.

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, 2013. 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, 2013

a) Government-Wide Financial Statements

The GWFS are composed of: (1) the statements of net position (SNP) 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, 2013. 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 Position

The purpose of SNP 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 SNP is presented as *net position*, 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 position, 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 position changed during the fiscal year ended June 30, 2013, 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 position*, which is essentially the same concept.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

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, 2013

FINANCIAL ANALYSIS OF GOVERNMENT-WIDE FINANCIAL STATEMENTS

The Municipality's overall financial position and operations at June 30, 2013 and 2012 are summarized as follows, based on the information included in the accompanying statement of net position:

	Governmental activities		Change	
	2013	2012	\$	%
Assets:				
Current assets	\$9,509,115	\$9,340,639	\$168,476	2%
Non-current assets:				
Capital assets, net	22,413,405	22,988,074	(574,669)	(2%)
Total assets	<u>31,922,520</u>	<u>32,328,713</u>	<u>(406,193)</u>	<u>(1%)</u>
Liabilities:				
Current liabilities, excluding long-term obligations	4,867,892	5,444,818	(576,926)	(11%)
Long-term obligations:				
Due within one year	3,228,691	3,176,064	52,627	2%
Due after one year	27,225,261	26,321,741	903,520	3%
Total liabilities	<u>35,321,844</u>	<u>34,942,623</u>	<u>379,221</u>	<u>(1%)</u>
Net position (deficit):				
Invested in capital assets, net of related debt	16,567,699	17,680,009	(1,112,310)	(6%)
Restricted	8,053,770	5,726,377	2,327,393	41%
Unrestricted	(28,020,793)	(26,020,296)	(2,000,497)	8%
Total net position	<u>\$(3,399,324)</u>	<u>\$(2,613,910)</u>	<u>\$ (785,414)</u>	<u>30%</u>

At June 30, 2013, the Municipality's current assets, amounting to \$9,509,115 are mainly composed of restricted and unrestricted cash and cash equivalents (\$930,882), restricted cash with fiscal agent (\$7,306,888), and restricted and unrestricted intergovernmental grants and contributions receivable (\$1,043,000).

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 \$22,413,405 at June 30, 2013, are substantially composed of capital assets, with a cost basis of \$32,202,934, which are reported net of accumulated depreciation and amortization of \$9,789,529.

**MUNICIPALITY OF SANTA ISABEL,
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Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

At June 30, 2013, the Municipality's current liabilities (excluding current portion of long-term liabilities) amounting to \$4,867,892 are mainly composed of unearned revenues (\$1,404,012), accounts payable and accrued liabilities (\$1,406,064), and intergovernmental payables (\$1,612,019). Unearned revenues are 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 \$30,453,952 at June 30, 2013, are mainly composed of current portion obligations (\$793,000 and \$2,435,691), the portion due after one year of bonds and notes payable (\$23,639,500) and the estimated landfill closure and post closure care costs (\$3,260,000).

As noted earlier, net position may serve over time as a useful indicator of the Municipality's financial position. The liabilities of the Municipality exceeded assets by (\$3,399,324) at June 30, 2013. The most significant portion of net position (\$16,567,699) 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 position at June 30, 2013, represents resources that are restricted for debt service payments (\$5,450,137) and for other specified purposes (\$2,603,633).

The remaining component of total net position consists of unrestricted net liabilities amounting to (\$28,020,793) at June 30, 2013. 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 position of the Municipality decreased by \$785,414 for the fiscal year ended June 30, 2013. Such decrease is due to the excess of total expenses (\$20,300,845), including depreciation and amortization of capital assets of (\$949,129), over total revenues (\$19,515,431) for the fiscal year ended June 30, 2013.

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**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

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, 2013 and 2012:

	Governmental activities		Change	
	2013	2012	\$	%
Program revenues:				
Program-specific operating grants and contributions	\$1,128,441	\$1,333,386	\$ (204,945)	(15%)
Program-specific capital grants and contributions	2,279,879	2,373,726	(93,847)	(4%)
Charges for services	2,435,604	674,180	1,761,424	261%
Total program revenues	<u>5,843,924</u>	<u>4,381,292</u>	<u>1,462,632</u>	<u>33%</u>
General revenues:				
Property taxes	3,562,954	4,178,828	(615,874)	(15%)
Municipal license taxes	1,492,285	1,610,585	(118,300)	(7%)
Sales and use taxes	614,925	748,521	(133,596)	(18%)
Construction excise taxes	2,440,028	2,256,482	183,546	8%
Unrestricted grants and contributions	5,148,330	4,810,200	338,130	7%
Other general revenues (various sources)	412,985	327,457	85,528	26%
Total general revenues	<u>13,671,507</u>	<u>13,932,073</u>	<u>(260,566)</u>	<u>(2%)</u>
Total revenues	<u>19,515,431</u>	<u>18,313,365</u>	<u>1,202,066</u>	<u>7%</u>
Program expenses:				
General government	6,701,803	6,268,742	433,061	7%
Urban and economic development	8,135,140	9,913,526	(1,778,386)	(18%)
Public safety	734,354	715,630	18,724	3%
Health and sanitation	1,635,516	922,443	713,073	77%
Culture, recreation and education	1,556,690	1,599,189	(42,499)	(3%)
Welfare and housing assistance	633,362	961,315	(327,953)	(34%)
Interest on long-term obligations	903,980	903,213	767	0%
Total expenses	<u>20,300,845</u>	<u>21,284,058</u>	<u>(983,213)</u>	<u>(5%)</u>
Net increase (decrease) in net position	(785,414)	(2,970,693)	2,185,279	(74%)
Net position, at beginning of fiscal year, as restated	(2,613,910)	356,783	(2,970,693)	(833%)
Net position, at end of fiscal year	<u>\$(3,399,324)</u>	<u>\$ (2,613,910)</u>	<u>\$ (785,414)</u>	<u>30%</u>

As previously mentioned, the Municipality's total net position decreased by \$785,414 during the current fiscal year. Approximately 41% (\$8,110,192) of the Municipality's total revenues for the current fiscal year came from property, municipal license, construction excise and sales and use taxes, while 44% (\$8,556,650) resulted from restricted and unrestricted capital and operating grants and contributions. Charges for services and other revenues, amounting to \$2,848,589, provided 15% 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, 2013

The Municipality's expenses cover a wide range of services. The largest expenses of the Municipality for the fiscal year ended June 30, 2013 were related to: (1) general administrative and operating costs (\$6,701,803), which were classified as "general government" and accounted for 33% of total expenses, (2) welfare and housing assistance (\$633,362), which accounted for 3% of total expenses, (3) health and sanitation (\$1,635,516), which accounted for 8% of total expenses, (4) urban and economic development (\$8,135,140), which accounted for 40% of total expenses, (5) public safety (\$734,354), which accounted for 4% of total expenses, (6) culture, recreation and education (\$1,556,690), which accounted for 8% of total expenses, and (7) interest on long-term obligations (\$903,980), which accounted for 4% of total expenses. These expenses include depreciation of capital assets in the amount of \$949,129, for the fiscal year ended June 30, 2013.

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, 2013, the total assets of governmental funds amounted to \$12,185,253, which consisted of: (1) cash and cash equivalents of \$930,882; (2) cash in fiscal agent of \$7,306,888; (3) Due from other funds of \$2,676,138, and; (4) property and sales taxes, intergovernmental, and other receivables of \$1,271,345. Such assets include cash, cash equivalents and receivables that are principally used for debt service, capital projects and other specific purposes.

At June 30, 2013, the total liabilities of governmental funds amounted to \$8,290,030, which consisted of: (1) unearned revenues of \$1,404,012; (2) accounts payable and accrued liabilities of \$1,406,064; (3) intergovernmental accounts payable of \$1,612,019; (4) Due to other funds of \$2,676,138, and; (5) matured bonds and interests due and payable of \$1,191,797.

At June 30, 2013, the total deferred inflows of resources of governmental funds amounted to \$360,929, which consisted of unavailable revenues.

The total fund balances of governmental funds amounted to \$3,534,294 at June 30, 2013, which are restricted for capital projects, debt service and other specific purposes. The fund balances of governmental funds increased by \$754,389 during the fiscal year ended June 30, 2013.

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**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

The following table presents the condensed financial position of governmental funds at June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Assets:		
Total assets - major governmental funds	\$ 10,897,527	\$ 9,540,957
Total assets - other governmental funds	1,287,726	1,088,901
Combined total assets	<u>12,185,253</u>	<u>10,629,858</u>
Liabilities:		
Total liabilities - major governmental funds	7,300,969	6,388,118
Total liabilities - other governmental funds	989,061	900,919
Combined total liabilities	<u>8,290,030</u>	<u>7,289,037</u>
Deferred Inflows of Resources:		
Total deferred inflows - major governmental funds	360,929	560,916
Total deferred inflows - other governmental funds	-	-
Combined total deferred inflows of resources	<u>360,929</u>	<u>560,916</u>
Fund balances (deficits):		
Restricted, Committed or Assigned – Major Funds	8,320,331	6,604,576
Restricted, Committed or Assigned – Other Funds	298,665	187,982
Unassigned	(5,084,702)	(4,012,653)
Combined total fund balances	<u>3,534,294</u>	<u>2,779,905</u>
Total liabilities, deferred inflows and resources and fund balances	<u>\$ 12,185,253</u>	<u>\$ 10,629,858</u>

Major Governmental Funds

General fund (GF) – The GF is the principal operating fund of the Municipality. The GF's total assets amounted to \$1,324,831 at June 30, 2013. Such assets consist principally of: (1) Cash in commercial banks (\$242,136), (2) sales and use tax receivables (\$123,837), (3) short-term amounts due from other funds (\$506,038), (4) due from governmental entities (\$360,929), and (5) restricted cash in fiscal agent (\$89,432).

The GF's total liabilities amounted to \$5,959,172 at June 30, 2013. Such liabilities are composed of: (1) unearned revenues (\$1,212,571), (2) due to other funds (\$2,169,695), and (2) accounts payable and accrued liabilities, including amounts due to other governments (\$2,576,906).

At the end of the current fiscal year, restricted fund balance amounted to \$89,432 and unassigned fund deficit amounted to (\$5,084,702).

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

State legislative joint resolutions fund (SLJRF)- The SLJRF's total assets amounted to \$2,454,968 at June 30, 2013, which consist of : (1) cash in commercial banks (\$285,273), and (2) due from other funds (\$2,169,695). The SLJRF's total liabilities amounted to \$150,000 at June 30, 2013, which are composed of accounts payable. At the end of the current fiscal year, the SLJRF had total restricted fund balances amounted to \$2,304,968.

Capital improvement bond fund (CIBF)- The CIBF's total assets amounted to \$1,221,794 at June 30, 2013, which consist of restricted cash with fiscal agent. The CIBF's did not have liabilities at June 30, 2013. At the end of the current fiscal year, the CIBF had total restricted fund balances amounted to \$1,221,794.

Debt service fund (DSF)- The DSF's total assets amounted to \$5,895,934 at June 30, 2013, which consist mainly of restricted cash in fiscal agent (\$5,809,055). The DSF's total liabilities amounted to \$1,191,797 at June 30, 2013, which are composed of: (1) matured bonds due and payable (\$746,000), and (2) matured interest due and payable (\$445,797). At the end of the current fiscal year, DSF's total and restricted fund balance amounted to \$4,704,137.

Other governmental funds (OGF)- The OGF's total assets amounted to \$1,287,726 at June 30, 2013, which consist mainly of restricted cash and cash equivalents (\$403,473), cash in fiscal agent (\$186,607), and receivables from intergovernmental grants and contributions (\$682,071). The OGF's total liabilities amounted to \$989,061 at June 30, 2013, which are composed of unearned revenues (\$191,441), accounts payable and accrued liabilities (\$291,177) and short-term amounts due to other funds (\$506,443). At the end of the current fiscal year, OGF's total restricted fund balance amounted to \$298,665.

Analysis of Operating Results of Governmental Funds

Major Governmental Funds

General fund – The total fund deficit of the GF increased by (\$1,094,363) during current fiscal year. Total revenues, expenditures and net other financing sources (uses) amounted to \$12,643,621, \$14,734,719, and \$996,735, respectively, for the fiscal year ended June 30, 2013.

Approximately 47% (\$5,978,302) of the GF's total revenues for the current fiscal year came from property, municipal license, construction excise and sales and use taxes, while 41% (\$5,155,138) resulted from intergovernmental grants and contributions. Interest revenues, charges for services and miscellaneous revenues, amounting to \$1,510,181, provided 12% of the total revenues for the current fiscal year.

The largest expenses of the GF for the fiscal year ended June 30, 2013 were related to: (1) general administrative and operating costs (\$6,759,642), which were classified as "general government" and accounted for 46% of total expenses, (2) welfare and housing assistance (\$290,383), which accounted for 2% percent of total expenses, (3) health and sanitation (\$530,635), which accounted for 4% of total expenses, (4) urban and economic development (\$5,873,170), which accounted for 40% of total expenses, (5) public safety (\$511,560), which accounted for 3% of total expenses, and (6) culture, recreation and education (\$769,329), which accounted for 5% of total expenses.

State legislative joint resolutions fund (SLJRF)-The total fund balance of the SLJRF increased by \$1,123,175 during current fiscal year. Total revenues and expenditures amounted to 1,474,873 and \$351,698, respectively, for the fiscal year ended June 30, 2013. SLJRF's total revenues for the current fiscal year resulted principally from intergovernmental grants and contributions, and total expenditures came from urban and economic development.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

Capital improvement bond fund (CIBF)- The total fund balance of the CIBF decreased by \$287,641 during current fiscal year. Total expenditures amounted to \$792,641 for the fiscal year ended June 30, 2013, and came from urban and economic development.

Debt service fund (DSF) – The total fund balance of the DSF increased by \$902,535 during current fiscal year. Total revenues, expenditures and other financing sources (uses) amounted to \$2,310,250, \$1,665,980 and \$258,265, respectively, for the fiscal year ended June 30, 2013.

Approximately 60% (\$1,394,155) of DSF's total revenues for the current fiscal year came from restricted property taxes, while 40% (\$914,477) came from restricted sales and use taxes. DSF's total expenditures for the current fiscal year came from principal and interests on bonds payable (\$1,665,980).

Other governmental funds (OGF) – The total fund balance of the OGF increased by \$110,683 during current fiscal year. Total revenues and expenditures amounted to \$3,286,674 and \$3,175,991, respectively, for the fiscal year ended June 30, 2013. Approximately 49% (\$1,621,151) of OGF's total revenues for the current fiscal year came from intergovernmental grants, while 40% (\$1,301,534) came from charge for services.

The largest expenses of the OGF for the fiscal year ended June 30, 2013 were related to: (1) urban and economic development (\$1,020,758), which accounted for 32% of total expenses, (2) welfare and housing assistance (\$335,454), which accounted for 11% percent of total expenses, (3) health and sanitation (\$1,100,131), which accounted for 35% of total expenses, and (4) culture, recreation and education (\$576,354), which accounted for 18% of total expenses.

BUDGETARY HIGHLIGHTS

a) General Fund

The original and final budget of the general fund for the fiscal year ended June 30, 2013 amounted to \$12,068,875. 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, 2013 were \$12,582,506, which is \$513,631 greater than the budgeted revenues. In addition, the total actual expenditures (budgetary basis) of the general fund for the fiscal year ended June 30, 2013 were \$13,732,547, which is \$1,878,022 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 \$167,341, 660,075 and \$454,449 lower than budgeted, while actual revenues in property taxes, intergovernmental grants and contributions and charge for services exceeded budgeted revenues by \$232,202, \$361,728, and \$1,056,471, respectively.

Also, the most significant fluctuations in actual expenditures occurred in general government, which had actual expenditures that were \$1,365,821 more than budgeted, and in urban and economic development, which had actual expenditures that were \$749,173 more than budgeted.

**MUNICIPALITY OF SANTA ISABEL,
COMMONWEALTH OF PUERTO RICO**
Management's Discussion and Analysis
Fiscal Year Ended June 30, 2013

CAPITAL ASSETS AND DEBT ADMINISTRATION

a) Capital Assets

The Municipality has invested \$32,202,934 in capital assets used in governmental activities, which have an accumulated depreciation and amortization of \$9,789,529 at June 30, 2013. The net capital assets of governmental activities decreased during the current fiscal year due to the current fiscal year's capital additions (\$374,460), which were totally offset by the depreciation and amortization expense (\$949,129).

b) Debt Administration

The Municipality finances a significant portion of its construction activities through bond and note 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, 2013, the Municipality's total bonded debt amounted to \$24,432,500, 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, 2013.

- Bonds payable increased by \$1,160,000 by the net effect of total principal payments on bonds made during the current fiscal year (\$600,000), and the issuance of bonds during the current year (\$1,760,000).
- The Municipality has also certain outstanding notes payable due to Puerto Rico Treasury Department (\$96,076). 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 (\$860,982). Such notes payable decreased by \$32,940 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 Position
June 30, 2013

Assets

Current assets:

Cash in commercial banks	\$ 930,882
Cash with fiscal agent	7,306,888
Accounts receivable, net of allowance for doubtful accounts:	
Property taxes	19,775
Intergovernmental	1,043,000
Sales tax	190,941
Interest	2,459
Miscellaneous	15,170
Total current assets	9,509,115

Noncurrent assets:

Capital assets, net of accumulated depreciation and amortization of \$9,789,529	22,413,405
Total noncurrent assets	22,413,405
Total assets	\$ 31,922,520

Current Liabilities (due within one year):

Accounts payable	\$ 1,406,064
Intergovernmental payables	1,612,019
Accrued interest payable on long-term debt	445,797
Unearned revenues	1,404,012
Current portion of long-term obligations:	
Bonds payable	793,000
Other debts	2,435,691
Total current liabilities	8,096,583

Noncurrent liabilities (due in more than one year):

Total liabilities	27,225,261
	\$ 35,321,844

Net position:

Invested in capital assets, net of related debt	\$ 16,567,699
Restricted for:	
Debt service	5,450,137
Other specified purposes	2,603,633
Unrestricted	(28,020,793)
Total net position	\$ (3,399,324)

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, 2013

<u>Functions/programs</u>	<u>Expenses</u>	<u>Charges for services</u>	<u>Program Revenues</u>		<u>Net Expenses and Charges in Net Assets</u>
			<u>Operating grants and contributions</u>	<u>Capital grants and contributions</u>	
Governmental activities :					
General government	\$ 6,701,803	\$ -	\$ -	\$ -	\$ (6,701,803)
Urban and economic development	8,135,140	13,797	243,790	2,279,879	(5,597,674)
Public safety	734,354	53,009	-	-	(681,345)
Health and sanitation	1,635,516	2,368,798	-	-	733,282
Culture, recreation and education	1,556,690	-	569,230	-	(987,460)
Welfare and housing assistance	633,362	-	315,421	-	(317,941)
Interest on long-term obligation	903,980	-	-	-	(903,980)
Total governmental activities	<u>\$ 20,300,845</u>	<u>\$ 2,435,604</u>	<u>\$ 1,128,441</u>	<u>\$ 2,279,879</u>	<u>\$ (14,456,921)</u>
General Revenues:					
Taxes:					
Property taxes					3,562,954
Municipal license taxes					1,492,285
Sales taxes					614,925
Construction excise taxes					2,440,028
Total taxes					<u>8,110,192</u>
Grants and contributions, not restricted to specific programs					5,148,330
Interests on deposits					41,925
Miscellaneous					371,060
Total general revenues					<u>13,671,507</u>
Net changes in net position					(785,414)
Net position at beginning of the year					(2,613,910)
Net position at the end of the year					<u>\$ (3,399,324)</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, 2013

	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	\$ 242,136	\$ 285,273	\$ -	\$ -	\$ 403,473	\$ 930,882
Cash in fiscal agent	89,432	-	1,221,794	5,809,055	186,607	7,306,888
Account receivable, net of doubtful accounts:						
Property taxes	-	-	-	19,775	-	19,775
Sales tax	123,837	-	-	67,104	-	190,941
Interest	2,459	-	-	-	-	2,459
Other	-	-	-	-	15,170	15,170
Due from other funds	506,038	2,169,695	-	-	405	2,676,138
Due from governmental entities	360,929	-	-	-	682,071	1,043,000
Total assets	<u>\$ 1,324,831</u>	<u>\$ 2,454,968</u>	<u>\$ 1,221,794</u>	<u>\$ 5,895,934</u>	<u>\$ 1,287,726</u>	<u>\$ 12,185,253</u>
LIABILITIES						
Accounts payable	964,887	150,000	-	-	291,177	1,406,064
Intergovernmental	1,612,019	-	-	-	-	1,612,019
Due to other funds	2,169,695	-	-	-	506,443	2,676,138
Unearned revenue	1,212,571	-	-	-	191,441	1,404,012
Matured bonds due and payable	-	-	-	746,000	-	746,000
Matured interests due and payable	-	-	-	445,797	-	445,797
Total liabilities	<u>5,959,172</u>	<u>150,000</u>	<u>-</u>	<u>1,191,797</u>	<u>989,061</u>	<u>8,290,030</u>
DEFERRED INFLOWS OF RESOURCES						
Unavailable revenue	360,929	-	-	-	-	360,929
Total deferred inflows of resources	<u>360,929</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>360,929</u>
FUND BALANCE (DEFICIT)						
Fund Balance:						
Restricted	89,432	2,304,968	1,221,794	4,704,137	298,665	8,618,996
Unassigned	(5,084,702)	-	-	-	-	(5,084,702)
Total fund balances (deficit)	<u>(4,995,270)</u>	<u>2,304,968</u>	<u>1,221,794</u>	<u>4,704,137</u>	<u>298,665</u>	<u>3,534,294</u>
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE (DEFICIT)	<u>\$ 1,324,831</u>	<u>\$ 2,454,968</u>	<u>\$ 1,221,794</u>	<u>\$ 5,895,934</u>	<u>\$ 1,287,726</u>	<u>\$ 12,185,253</u>

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 Position
 June 30, 2013

Aggregate fund balance reported in the balance sheet - governmental funds	\$ 3,534,294
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	22,413,405
Deferred (unavailable) revenues in the governmental funds that are recorded as revenues in the statement of activities	360,929
The following liabilities are not due (mature) in the current period, therefore, are not reported in the governmental funds:	
Accrued employees' christmas bonus	(215,922)
Compensated absences	(1,588,472)
Bonds and notes payable	(23,686,500)
Debt to intergovernmental agencies	(957,058)
Landfill closure and postclosure care costs	<u>(3,260,000)</u>
Net position as reported in the accompanying statement of net position	<u>\$ (3,399,324)</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, 2013

	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	\$ 2,345,541	\$ -	\$ -	\$ 1,394,155	\$ -	\$ 3,739,696
Municipal license	1,492,285	-	-	-	-	1,492,285
Construction excise taxes	614,925	-	-	-	-	614,925
Sales tax	1,525,551	-	-	914,477	-	2,440,028
Charges of service	1,125,971	-	-	-	1,301,534	2,427,505
Intergovernmental grants and contributions:						
Federal government	-	-	-	-	1,621,151	1,621,151
State government	5,155,138	1,473,414	-	-	330,192	6,958,744
Investment earnings	40,307	-	-	1,618	-	41,925
Miscellaneous	343,903	1,459	-	-	33,797	379,159
Total Revenues	\$ 12,643,621	\$ 1,474,873	\$ -	\$ 2,310,250	\$ 3,286,674	\$ 19,715,418
EXPENDITURES						
Current:						
General government	6,759,642	-	-	-	-	6,759,642
Urban and economic development	5,873,170	351,698	792,641	-	1,020,758	8,038,267
Public safety	511,560	-	-	-	143,294	654,854
Health and Sanitation	530,635	-	-	-	1,100,131	1,630,766
Culture, recreation and education	769,329	-	-	-	576,354	1,345,683
Welfare and housing assistance	290,383	-	-	-	335,454	625,837
Debt service:						
Principal	-	-	-	762,000	-	762,000
Interest	-	-	-	903,980	-	903,980
Total Expenditures	14,734,719	351,698	792,641	1,665,980	3,175,991	20,721,029
Excess (Deficiency) of Revenues over expenditures	(2,091,098)	1,123,175	(792,641)	644,270	110,683	(1,005,611)
OTHER FINANCING SOURCES (USES)						
Transfer in from other funds	-	-	-	258,265	-	258,265
Transfer out to other funds	(258,265)	-	-	-	-	(258,265)
Proceeds from bond issuance	1,255,000	-	505,000	-	-	1,760,000
Total Other Financing Sources (uses)	996,735	-	505,000	258,265	-	1,760,000
NET CHANGE IN FUND BALANCES (DEFICITS)	(1,094,363)	1,123,175	(287,641)	902,535	110,683	754,389
FUND BALANCE (DEFICIT) AT BEGINNING OF YEAR	(3,900,907)	1,181,793	1,509,435	3,801,602	187,982	2,779,905
FUND BALANCE (DEFICIT) AT END OF YEAR	\$ (4,995,270)	\$ 2,304,968	\$ 1,221,794	\$ 4,704,137	\$ 298,665	\$ 3,534,294

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

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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, 2013

Net change in fund balances- total governmental funds \$ 754,389

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	(176,742)
Net Change in State Treasury Department Christmas Bonus Reimbursement Deferred in GFFS	(23,245)

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	(71,290)
Net Change in Christmas Bonus	50,047
Other intergubernamental debts	254,096

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. (574,669)

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 762,000

Proceeds on issuance of long- term debt (bonds) are recorded as other financing sources in the fund financial statements, but the issuances increase long-term liabilities in the statement of net assets (1,760,000)

Net changes in net position reported in the accompanying statements of activities \$ (785,414)

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, 2013

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, 2013, 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, 2013 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).

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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, 2013, 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, 2013.

b) *Financial Reporting Entity*

A financial reporting entity consists of a primary government and its component units. Accordingly, for financial reporting purposes, the primary government is the Municipality. In accordance with GASB No. 14 and GASB No. 61, the criteria used to determine whether organizations are to be included as component units within the Municipality's financial reporting entity are as follow: (1) The organization is legally separate entity; (2) The Municipality appoints a voting majority of the organization's board; (3) There is a financial benefit/burden relationship between the Municipality and the organization or the Municipality is able to impose its will on the organization.

Organizations meeting the above criteria are included in the Municipality's financial reporting entity as discretely presented component units. Entities which meet any of the following in addition to the above criteria are considered to be blended component units of the Municipality: (1) The organization's governing body is substantively the same as the Municipality's governing body and (a) there is a financial benefit or burden relationship between the Municipality and the organization, or (b) management of the Municipality has operational responsibility for the organization; (2) The organization provides services entirely, or almost entirely, to the Municipality, or otherwise exclusively, or almost exclusively, benefits the Municipality even though it does not provide services directly to it; (3) The organization's total debt outstanding, including leases, is expected to be repaid entirely or almost entirely with Municipality resources.

Legally separate organizations that do not otherwise meet the criteria for inclusion as a component unit may be included in the financial reporting entity if it is determined that their exclusion would render the financial statements misleading. This determination is bases on the nature and significance of the organization's relationship with the Municipality.

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

c) Government-Wide Financial Statements

The accompanying GWFS are composed of: (1) the statement of net position 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 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 position provides short-term and long-term information about the Municipality's financial position and condition by presenting all of the Municipality's assets, deferred outflow of resources, liabilities and deferred inflow of resources, with the difference between these items reported as "net position" (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 position are classified in the accompanying statement of net position with in 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.

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- **Restricted net position** – These consist of net position restricted by external parties (such as creditors, grantors, contributors, laws or regulations of other governments, etc.), or net position 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 position identifies resources that have been received or earned by the Municipality with an explicit understanding between the Municipality 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 position. 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 position** – These consist of net position that are neither externally or legally restricted, nor invested in capital assets. However, unrestricted net position often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net position 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 position or liabilities changed during the fiscal year ended June 30, 2013, 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:

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General Government:

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

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:

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- **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 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 position and activities.

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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 position 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.

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 with in 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.

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- **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 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, 2013, 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 position. 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.

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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, deferred outflows of resources, liabilities, deferred inflows of resources, 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 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.

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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 position, 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 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.

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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 an other 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.
- 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 position. 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.

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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, 2013, 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 unearned revenues at June 30, 2013.

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 both measurability and availability criteria in the accompanying governmental fund financial statements, except for amounts recorded as unearned 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.

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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. GASB 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.

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, 2013, which have been recorded as governmental fund liabilities at June 30, 2013, 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 position. 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.

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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 position 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 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.

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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.

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.

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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, 2013. 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, 2013.

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 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.

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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 non interest 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, 2013. 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 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 position. 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 position. 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 position, 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.

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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 position 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.

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.

i) Unearned Revenues

In the governmental fund financial statements, unearned revenue arises when 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 unearned revenue is removed and revenue is recognized.

Unearned revenues at the government-wide level arise only when the Municipality receives resources before it has a legal claim to them (reported as “*unearned revenue*” in the accompanying statement of net position).

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j) Deferred Outflow/Inflow of Resources

In addition to assets, the statement of net position and governmental funds balance sheet will sometimes report a separate section for deferred outflow of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position or fund balance that applies to a future period (s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The Municipality has no deferred outflows of resources.

In addition to liabilities, the statement of net position and governmental funds balance sheet will sometimes report a separate section for deferred inflow of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position or fund balances that applies to a future period (s) and so will not be recognized as an inflow of resources (revenue) until that time. The Municipality has only one type of item, which arises only under a modified accrual basis of accounting that qualifies for reporting in this category. Accordingly, the item "earned and unavailable revenue" is reported only in the governmental funds balance sheet. The governmental funds reports unavailable revenues from intergovernmental grants and contributions. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available.

k) Compensated Absences

The liability for compensated absences recorded in the accompanying statement of net position is limited to leave that: (1) is attributable to services already rendered on or before June 30, 2013 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.

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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 position. 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 position include the Municipality's bonds payable, notes payable, obligations under capital leases, accrued compensated absences and accrued legal claims and judgments.

All long-term debt to be repaid from governmental resources is reported as liabilities in the accompanying statement of net position. 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 position, 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 System2000, the two retirement systems in which the employees of the Municipality participate. Accordingly, the Municipality is considered a participant and not as ponsor of these retirement systems since the majority of the participants in the aforementioned pension trustfunds 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.

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According to GASB No. 27, the Municipality accounts for pension costs from the stand point 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.

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, 2013 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.

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The current insurance policies have not been cancelled or terminated at June 30, 2013. 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:

- ***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 Municipal's highest level of decision making authority (Municipal Legislature through resolutions and ordinances) and can only be changed by a similar law, ordinance or resolution, no later than the end of fiscal year.
- ***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.

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- **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, 2013.

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.

At June 30, 2013, the accompanying fund financial statements reported fund balances as restricted and unassigned.

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.

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- **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.

r) Future Adoption of Accounting Pronouncements

The GASB has issued the following standards that have effective dates after June 30, 2013:

- 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.

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- 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.
- 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.
- GASB Statement No. 71 *Pension Transition for Contributions Made Subsequent to the Measurement Date—an amendment of GASB Statement No. 68 (Issued 11/13)*. The objective of this Statement is to address an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The provisions of this Statement are required to be applied simultaneously with the provisions of Statement 68.

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

s) Adoption of New Accounting Pronouncements

The provisions of the following Governmental Accounting Standards Board (GASB) Statement have been implemented for the year ended June 30, 2013:

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- GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources.
- GASB Statement No. 65, Items 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.

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, 2013.

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- **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, 2013, (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, 2013, the interest rate risk associated with the Municipality’s cash and cash equivalent is considered low.

- **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 \$7,306,888 at June 30, 2013, are uninsured and uncollateralized. However, no losses related to defaults by GDB on deposit transactions have been incurred by the Municipality through June 30, 2013. 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, 2013, 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, 2013.

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, 2013. 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	\$ 242,136	\$ 285,273	\$ -	\$ -	\$ 403,473	\$ 930,882
Cash in GDB, as fiscal agent	89,432	-	1,221,794	5,809,055	186,607	7,306,888
Total carrying amount of deposits	<u>\$ 331,568</u>	<u>\$ 285,273</u>	<u>\$ 1,221,794</u>	<u>\$ 5,809,055</u>	<u>\$ 590,080</u>	<u>\$ 8,237,770</u>

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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, 2013, 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 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 \$1,212,571 at June 30, 2013, which represents municipal licenses collected in advance for the taxable year 2013-2014.

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, 2013, 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.

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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.

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, 2013, of \$123,837 and \$67,104, 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.

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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.

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, 2013 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, 2013 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.

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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.

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 position
<i>Intergovernmental receivables:</i>				
Grants and contributions:				
Puerto Rico Department of Labor – Act. No. 52	\$ -	\$ 273,585	\$ 273,585	\$ 273,585
Puerto Rico Administration for Integral Care and Development of Children		107,289	107,289	107,289
Puerto Rico Office of the Commissioner of Municipal Affairs	-	194,913	194,913	194,913
Puerto Rico Treasury Department – Christmas bonus	100,289	-	100,289	100,289
Puerto Rico Municipal Revenue Collection Center	260,640	-	260,640	260,640
Others	-	106,284	106,284	106,284
Total intergovernmental receivables	<u>\$ 360,929</u>	<u>\$ 682,071</u>	<u>\$ 1,043,000</u>	<u>\$ 1,043,000</u>
<i>Intergovernmental payables:</i>				
Puerto Rico Treasury Department	\$ 19,757	\$ -	\$ 19,757	\$ 19,757
Employees Retirement System of the Government of the Commonwealth of Puerto Rico	451,219	-	451,219	451,219
Puerto Rico Department of Labor	335,950	-	335,950	335,950
Puerto Rico Aqueduct and Sewer Authority	603,125	-	603,125	603,125
Puerto Rico Energy Power Authority	22,679	-	22,679	22,679
Social Security Administration	33,146	-	33,146	33,146
Puerto Rico General Services Administration	2,081	-	2,081	2,081
Commonwealth of Puerto Rico Employees Association	144,062	-	144,062	144,062
Total intergovernmental payables	<u>\$ 1,612,019</u>	<u>\$ -</u>	<u>\$ 1,612,019</u>	<u>\$ 1,612,019</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 (\$100,289) and (\$260,640) from Puerto Rico Municipal Revenue Collection Center are recorded as unavailable 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, 2013 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	\$ -	2,169,695	-	\$ 2,169,695
Non-major governmental funds:	506,038	-	405	506,443
Total	\$ 506,038	2,169,695	405	\$ 2,676,138
Transfers out:				
Transfers in:	General fund	Total governmental funds		
Major governmental funds:				
Debt service fund	\$ 258,265	\$ 258,265		
Total	\$ 258,265	\$ 258,265		

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 2013.

Inter-fund receivables and payables represent the pending settlements of the aforementioned transfers at June 30, 2013.

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8. Capital Assets

Capital assets activity of the governmental activities for the fiscal year ended June 30, 2013 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	-	-	-	-
Total capital assets, not being depreciated	<u>1,433,191</u>	<u>-</u>	<u>-</u>	<u>1,433,191</u>
Capital assets, being depreciated:				
Buildings, structures and buildings improvements	20,387,039	-	-	20,387,039
Infrastructure	5,283,512	-	-	5,283,512
Land improvements	62,800	-	-	62,800
Licensed vehicles	2,709,349	239,739	-	2,949,088
Machinery and equipment	1,985,975	134,721	-(33,392)	2,087,304
Total capital assets, being depreciated	<u>30,428,675</u>	<u>374,460</u>	<u>(33,392)</u>	<u>30,769,743</u>
Total cost basis of capital assets	<u>\$ 31,861,866</u>	<u>\$ 374,460</u>	<u>\$ (33,392)</u>	<u>\$ 32,202,934</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	\$ 3,706,947	\$ 425,550	\$ -	\$ 4,132,497
Infrastructure	2,024,387	185,849	-	2,210,236
Land improvements	9,230	1,130	-	10,360
Licensed vehicles	2,111,791	168,075	-	2,279,866
Machinery and equipment	1,021,437	168,525	(33,392)	1,156,570
Total accumulated depreciation	<u>8,873,792</u>	<u>949,129</u>	<u>(33,392)</u>	<u>9,789,529</u>
Net capital assets, governmental activities	<u>\$ 22,988,074</u>	<u>\$ (574,669)</u>	<u>\$ -</u>	<u>\$ 22,413,405</u>

The Municipality did not have complete and accurate accounting records of capital assets at June 30, 2013.

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Depreciation and amortization expense of governmental activities for the fiscal year ended June 30, 2013 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	\$ 949,129

9. Unearned Revenues

At June 30, 2013, unearned 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 position
<i>Unearned revenues:</i>				
Municipal licenses	\$ 1,212,571	\$ -	\$ 1,212,571	\$ 1,212,571
Intergovernmental grants and contributions	-	191,441	191,441	191,441
Total unearned revenues	\$ 1,212,571	\$ 191,441	\$ 1,404,012	\$ 1,404,012

10. Deferred Outflow/Inflow of Resources

At June 30, 2013, measurable and unavailable revenues recorded in the GWFS and the governmental fund financial statements are as follows:

	General Fund	Total governmental funds	Statement of net position
<i>Earned and unavailable revenues:</i>			
CRIM Final Settlement	\$ 260,640	\$ 260,640	\$ -
Intergovernmental grants and contributions	100,289	100,289	-
Total unavailable revenues	\$ 360,929	\$ 360,929	-

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11. Long-Term Obligations

The general long-term debt activity for the fiscal year ended June 30, 2013 is as follows:

	Balance at June 30, 2012	Borrowings or Additions	Payments or Deductions	Balance at June 30, 2013	Due Within One Year
Bonds and bond anticipation notes payables	\$23,272,500	\$ 1,760,000	\$ 600,000	\$24,432,500	\$ 793,000
Notes payable to:					
Puerto Rico Treasury Department					
Financing agreement to settle two legal demands	288,231	-	192,155	96,076	96,076
CRIM:					
Advances over collections through fiscal year 2000	475,183	-	12,003	463,180	12,756
Act No. 146 -Financing of delinquent property tax accounts sold	418,739	-	20,937	397,802	20,937
Compensated absences	1,517,183	945,770	874,481	1,588,472	950,000
Estimated landfill closure and post closure care costs	3,260,000	-	-	3,260,000	1,140,000
Christmas bonus	265,969	215,922	265,969	215,922	215,922
Total	<u>\$ 29,497,805</u>	<u>\$ 2,921,692</u>	<u>\$ 1,965,545</u>	<u>\$ 30,453,952</u>	<u>\$ 3,228,691</u>

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, 2013:

<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%	\$ 1,425,000
\$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%	565,000
\$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%	10,000
\$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%	130,000
\$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%	67,000

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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%	72,000
\$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%	133,500
\$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%	345,000
\$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%	555,000
\$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%	140,000
\$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%	140,000
\$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%	229,000
\$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%	1,075,000
\$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%	2,400,000
\$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%	35,000

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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%	640,000
\$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%	4,976,000
\$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%	780,000
\$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%	6,320,000
\$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%	2,635,000
\$1,255,000 general obligation bond series of 2013 payable in annual installments ranging of \$145,000 to \$220,000 through July 2019, interest ranging 6.00% to 7.50%	1,255,000
\$505,000 general obligation bond series of 2013 payable in annual installments ranging of \$5,000 to \$40,000 through July 2037, interest ranging 6.00% to 7.50%	505,000
Total bonds	<u>\$ 24,432,500</u>

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

Fiscal year ending June 30,	Principal	Interest
2014	\$ 793,000	\$ 987,691
2015	806,000	1,547,427
2016	864,000	1,492,173
2017	896,000	1,433,052
2018	954,000	1,371,343
2019-2023	4,786,500	5,867,202
2024-2028	5,846,000	4,338,223
2029-2033	6,767,000	2,192,950
2034-2038	2,720,000	239,450
Totals	<u>\$ 24,432,500</u>	<u>\$ 19,469,511</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, 2013, the outstanding balance of this note amounted to \$96,076, which is due on fiscal year 2013-2014.

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.

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.

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The outstanding principal balances of the note payable to CRIM amounted \$463,180, at June 30, 2013. The principal and interest maturities are as follows:

Fiscal year ending June 30,	Principal	Interest
2014	\$ 12,756	\$ 28,465
2015	13,558	27,663
2016	14,410	26,811
2017	15,315	25,906
2018	16,278	24,944
2019-2023	98,076	108,030
2024-2028	133,010	73,096
2029-2033	159,777	25,716
Totals	<u>\$ 463,180</u>	<u>\$ 340,631</u>

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, 2013, the outstanding principal balances amounted to \$397,802. The principal and interest maturities are as follows:

Fiscal year ending June 30,	Principal	Interest
2014	\$ 20,937	\$ 24,744
2015	20,937	23,442
2016	20,937	22,138
2017	20,937	20,836
2018	20,937	19,534
2019-2023	104,685	78,138
2024-2028	104,685	45,580
2029-2033	83,747	13,022
Totals	<u>\$ 397,802</u>	<u>\$ 247,434</u>

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e) *Compensated Absences*

At June 30, 2013, the government-wide statement of net position – governmental activities includes a liability amounting \$1,588,472, of which \$876,149 represents accrued sick leave benefits, and \$712,323 represents accrued vacation benefits, representing the Municipality's commitment to fund such costs from future operations.

12. **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.

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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Basic Financial Statements
June 30, 2013

- ***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.
- (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.

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- ***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.

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.

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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 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.

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June 30, 2013

• *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.

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:

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:

COMMONWEALTH OF PUERTO RICO
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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.

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>
2013	\$ 271,525	\$ 210,725	\$ 482,250
2012	273,238	211,525	484,763
2011	252,897	198,522	451,419
Totals	<u>\$ 797,660</u>	<u>\$ 620,772</u>	<u>\$ 1,418,432</u>

During the fiscal years ended June 30, 2013, 2012, and 2011, 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. Francisco Del Castillo Orozco, Interim 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.

13. 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. The Municipality reports \$3,260,000 as landfill closure and post-closure liability at June 30, 2014 based on 100% use of the total capacity of the landfill. Based on the fact that the landfill was closed in September 2013, the liability was fully recognized as of June 30, 2013. Actual costs may be higher or lower due to inflation, changes in technology, or changes in regulations.

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In 2011, the Municipality entered an Administrative Order on Consent (Docket No. RCRA-02-2011-7303) with the United States Environmental Protection Agency (“EPA”). The Municipality’s shall perform the actions required by this Order and comply with its provisions. This Order require, within others requirements, the following works:(1) revise the closure and post closure plans; (2) cover and maintain the landfill with an intermediate cover until a final cover is installed;(3) permanent closure of the entire Landfill no later than December 31, 2013; (4) carry out the post closure plan provisions as approved by the EPA; and (5) develop and implement a recycling and green waste management program. The Municipality have an obligation under the Administrative Order on Consent to comply with any requirement, term, or condition, set forth in or required by this Order, and is subject to penalties for failure to comply, unless the performance is prevented or delayed by events arising from causes not reasonably foreseeable and beyond the control of the Municipality.

14. Commitments, Contingencies and Uncertainties

Encumbrances

The Municipality has reported, outstanding encumbrances amounting to \$209,663 in the general fund at June 30, 2013. 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.

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, 2013. 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.

Construction

The Municipality had commitments at June 30, 2013 of approximately \$357,960 for the construction, improvements, or renovation of several capital facilities and the capital assets.

COMMONWEALTH OF PUERTO RICO
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June 30, 2013

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

15. Fund Balance (Deficit)

As of June 30, 2013, 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	\$ 89,432	\$ 2,304,968	\$ 1,221,794	\$ -	\$ -	\$ 3,616,194
Public safety	-	-	-	-	16,491	16,491
Health and sanitation	-	-	-	-	175,854	175,854
Culture and recreation and education	-	-	-	-	47,727	47,727
Welfare and housing assistance	-	-	-	-	58,593	58,593
Debt service	-	-	-	4,704,137	-	4,704,137
<i>Unassigned</i>	(5,084,702)	-	-	-	-	(5,084,702)
Total fund balances (deficit)	<u>\$ (4,995,270)</u>	<u>\$ 2,304,968</u>	<u>\$ 1,221,794</u>	<u>\$ 4,704,137</u>	<u>\$ 298,665</u>	<u>\$ 3,534,294</u>

16. Subsequent Events

On May 2014, the Municipality's Legislature approved Ordinance Number 18, authorizing the issuance of General Obligation Bonds in the amount of \$3,555,000. The net proceeds will be used to carry out certain capital improvements authorized by law. The interest rate on the bond will be prime rate 1.50 percent and maturity date is July 1, 2033. This bond is payable with resources collected through the Municipal Redemption Fund.

In accordance with Administrative Order (Docket No. RCRA-0-2011-7303) with the United States Environmental Protection Agency ("EPA"), the Municipality performed the following actions:

- (a) On September 30, 2013, the Municipality ceased receiving any waste for deposit in the Landfill and depositing waste in the final third of the Landfill, and;
- (b) On December 31, 2013, the Municipality permanently close the entire Landfill.

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June 30, 2013

On April 4, 2013, the Governor of the Commonwealth of Puerto Rico signed into law Act 3 of 2013 (Act 3), which adopted a comprehensive reform of the Employees Retirement System of the Commonwealth of Puerto Rico (ERS), the largest of the three Commonwealth retirement systems that are funded primarily with budget appropriations from the Commonwealth's General Fund. The ERS financial situation was approached through Act 3, which became effective on July 1, 2013 ("Effective Date"). The Act establishes the following: (i) it freezes and grandfatheres the benefits that have accrued through June 30, 2013 of those participants who are covered by the ERS's defined benefit formula (those who joined the ERS prior to January 1, 2000 whose retirement benefits accrued at a rate of 1.5% or 2% per year of creditable service) (the "Defined Benefit Employees"); (ii) it provides that, beginning on July 1, 2013, the retirement benefits accruing on and after the Effective Date for Defined Benefit Employees will be based on a defined contribution plan and will be paid out in the form of a lifetime annuity (upon retirement, the employee will receive the benefits accrued through June 30, 2013 based on the defined benefit formula plus the contributions made by the employee after June 30, 2013 in the form of a lifetime annuity); (iii) it provides that defined contribution benefits accrued pursuant to System 2000 will also be paid in the form of a lifetime annuity rather than a lump sum payment; (iv) it eliminates the so called "merit pension" that provided to participants who joined the Employees Retirement System prior to April 1, 1990, after attaining 30 years of service, a retirement benefit of 65% (if less than 55 years of age) or 75% (if age 55 or greater) of the average salary earned during the highest 36 months of employment; (v) it increases the retirement age for various groups of participants; (vi) it increases the employee contribution to the ERS from 8.275% to a minimum of 10%; (vii) it eliminates or reduces various retirement benefits previously granted by special laws and the System will benefit from the savings generated; (viii) it increases the minimum pension from \$400 to \$500 per month for current retirees; and (ix) it eliminates or modifies other benefits, such as disability and survivor benefits.

On June 30, 2013, the Commonwealth of Puerto Rico enacted Acts No. 40 through No. 48 (also known as the Comprehensive Tax Reform Acts), which amended the following Acts, Regulations and Codes: 1) the Puerto Rico Insurance Code under Act No. 77 of June 19, 1957, as amended, 2) the Property Tax Act under Act No. 83 of 1991, 3) the Savings and Loans Cooperatives Act under Act No. 255 of 2002, as amended, 4) the Puerto Rico Sales Tax Financing Corporation (COFINA) Act under Act No. 91 of 2006, 5) several articles of Act No. 1 of 2011 (also known as the Internal Revenue Code for a New Puerto Rico), 6) the Fiscal Reform Act of 2006 under Act No. 103 of 2006, 7) Act No. 164 of 2001, and 8) Act No. 221 of May 15, 1948. All these amendments are designed to achieve, among other things, an expansion of the revenue base of the general fund of the Commonwealth of Puerto Rico, and are expected to bring additional and consistent tax revenue. The aforementioned amendments involve, among other changes, the imposition of the sales and use taxes to certain business to business transactions, as defined, previously excluded, and other procedural changes (Acts No's. 40 and 42).

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Notes to Basic Financial Statements
June 30, 2013

On January 24, 2014, the Commonwealth of Puerto Rico enacted Act No. 18 (also known as the Municipal Administration Fund Act), to set up a special fund called the Municipal Administration Fund, which authorize municipalities to pledge the funds deposited on the Municipal Administration Fund to secure the repayment of any loan, bond, promissory note or other evidence of debt, whose source of repayment are the funds deposited into the Special Fund and to meet any budgeted expenditure of the municipalities and any activity or project of the municipalities; authorize the Government Development Bank for Puerto Rico to make disbursements for the purposes set out in the approved Law; amend paragraph (b) of section 4020.01; amended paragraph (b) of section 4020.02, and amend paragraph (a) and repealing paragraph (e) of section 6080.14 of the law No. 1 - 2011, as amended, known as the "Internal Revenue Code for a new Puerto Rico", for the purposes of restructuring the sales and use tax so that tax rate is six (6) percent statewide and one (1) percent at municipal level; to establish mechanisms for advances of the tax to the municipalities; and for other related purposes.

On January 24, 2014, the Commonwealth of Puerto Rico enacted Act No. 18 (also known as the Municipal Financing Corporation Act), to authorize the creation of a public corporation and instrumentality of the Commonwealth of Puerto Rico, attached to the Government Development Bank for Puerto Rico known as "Municipal Financing Corporation" (COFIM, by its acronyms in Spanish), with legal faculty to issue and/or use other mechanisms to pay or refinance the debt contracted by the municipalities, whose payment of principal and interest is supported by municipal sales and use taxes; establish that the first collections of municipal sales and use tax of one percent (1%) will be collected by municipalities and deposited directly to the Redemption Fund of the Municipal Financing Corporation; establish that bonds and obligations issued by the "Municipal Financing Corporation" will be payable and secured by the pledge of the greater of (i) a fixed amount of the municipal sales and municipal tax or (ii) the amount of the municipal sales and use tax fixed at zero point three percent (0.3%) collected during the previous fiscal year; and amend the paragraph (c) of section 4050.06, amend paragraph (a) of section 4050.07, amend paragraph (a) and (b) of section 4050.08, amend paragraph (a) of section 4050.09, and amend paragraphs (b), (c) and (d), repeal paragraph (e) and renumber paragraph (f) as (e) of section 6080.14 of the Act 1-2011, as amended, known as the "Internal Revenue Code for a new Puerto Rico"; in order to establish mechanisms for advances of the tax to the municipalities; and for other related purposes.

Management has evaluated subsequent events through November 16, 2014, which is the date the financial statements were available to be issued and determined that no material subsequent event require an estimate to be recorded as of June 30, 2013.

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, 2013

	<u>Budgeted amounts</u>		<u>Actual amounts</u>	<u>Variance with</u>
	<u>Original</u>	<u>Final</u>	<u>(budgetary</u> <u>basis)</u>	<u>final budget –</u> <u>over (under)</u>
Revenues:				
Property taxes	\$ 2,113,339	\$ 2,113,339	\$ 2,345,541	\$ 232,202
Sales and use taxes	1,980,000	1,980,000	1,525,551	(454,449)
Municipal license taxes	1,659,626	1,659,626	1,492,285	(167,341)
Construction excise taxes	1,275,000	1,275,000	614,925	(660,075)
Intergovernmental grants and contributions	4,793,410	4,793,410	5,155,138	361,728
Interest on deposits	70,000	70,000	40,307	(29,693)
Charges for services	69,500	69,500	1,125,971	1,056,471
Miscellaneous	108,000	108,000	282,788	174,788
Total revenues	<u>12,068,875</u>	<u>12,068,875</u>	<u>12,582,506</u>	<u>513,631</u>
Expenditures and encumbrances:				
General government	5,177,285	5,277,947	6,643,768	(1,365,821)
Urban and economic development	4,667,200	4,241,536	4,990,709	(749,173)
Public safety	597,828	598,612	487,787	110,825
Health and sanitation	565,304	565,304	531,059	34,245
Culture, recreation and education	536,411	825,105	780,348	44,757
Welfare and housing assistance	310,497	346,021	298,876	47,145
Total expenditures	<u>11,854,525</u>	<u>11,854,525</u>	<u>13,732,547</u>	<u>(1,878,022)</u>
Revenues over (under) expenditures and encumbrances	<u>214,350</u>	<u>214,350</u>	<u>(1,150,041)</u>	<u>(1,364,391)</u>
Other financing sources (uses):				
Transfer in from other governmental funds	-	-	-	-
Transfer out to other governmental funds	(214,350)	(214,350)	(214,350)	-
Total other financing sources (uses)	<u>(214,350)</u>	<u>(214,350)</u>	<u>(214,350)</u>	<u>-</u>
Net increase (decrease) in fund balance (deficit)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,364,391)</u>	<u>\$ (1,364,391)</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Budgetary Comparison Schedule- General Fund
(See Notes to Budgetary Comparison Schedule)
June 30, 2013

Reconciliation of differences:

Sources/inflows of financial resources:	
Actual amounts (budgetary basis) "available for appropriations" from the budgetary comparison schedule	\$ 12,582,506
Differences - budgetary basis to GAAP:	
Differences in bases of accounting:	
GAAP adjustments to revenues	61,115
Total revenues asreported on the statement of revenues, expenditures and changes in fund balances	<u>\$ 12,643,621</u>
Uses/outflows of financial resources:	
Actual amounts (budgetary basis) "total charges to appropriations" from the budgetary comparison schedule (including other financing uses)	\$ 13,732,547
Timing differences:	
Current year encumbrances recorded as expenditures for budgetary purposes	(209,663)
Prior year encumbrances recorded as expenditures for GAAP purposes	200,894
Entity differences:	
Non-budgeted expenditures	1,010,941
Total expenditures as reported on the statement of revenues, expenditures and changes in fund balances	<u>\$ 14,734,719</u>

See accompanying notes to financial statements.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
Notes to Budgetary Comparison Schedule- General Fund
June 30, 2013

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, 2013 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2013.

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

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

<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	\$ 26,199
Total U.S. Department of Agriculture			<u>26,199</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Program:			
Section 8 Housing Choice Voucher	14.871		289,723
Pass-Through State - Office of the Commissioner of Municipal Affairs:			
Community Development Block Grants – State’s Program	14.228	12-AB 11-AB-FC 10-AB-FC 09-AB-FC 08-AB-FC 06-FC 04-AB	<u>634,751</u>
Total U.S. Department of Housing and Urban Development			<u>924,474</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	FOA-00013-37	<u>77,639</u>
Total U.S. Department of Energy			<u>77,639</u>

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

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

<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 HOMELAND SECURITY:			
Pass-Through State – Office of the Governor:			
Disaster Grants- Public Assistance	97.036	N/AV	41,987
Pass-Through the Municipality of Ponce, P.R.			
Homeland Security Grant	97.067	N/AV	<u>28,691</u>
Total U.S. Department of Homeland Security			<u>70,678</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICE			
Pass-Through State – Administration of Children and Families:			
Child Care and Development Block Grant		241-2013-000066/ 241-2013-000171/ 241-2013-000171a	
	93.575		<u>543,215</u>
Total U.S. Department of Health and Human Service:			<u>543,215</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 1,642,205</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, 2013

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 AUDITOR'S 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**

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of 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, 2013, and the related notes to the financial statements. I was engaged to audit the financial statements of the governmental activities. These financial statements collectively comprise the Municipality's basic financial statements and have issued my report thereon dated November 16, 2014. I did not express an opinion on the governmental activities because I was unable to obtain sufficient and competent evidential matter related to the capital assets. Also, I issued a qualified opinion on the General Fund, the State Legislative Joint Resolutions Fund and the aggregate remaining fund because the Municipality did not maintain adequate accounting records of the interfund transactions and the corresponding due from and due to account balances. In addition, the opinion on the Capital Improvement Bonds Fund and the Debt Service Fund was unmodified. Finally, an emphasis of matter was included in the auditor report, related to an Administrative Order on Consent with the United States Environmental Protection Agency (EPA) in which the Municipality shall perform the actions required by this Order and the compliance with its provisions.

Internal Control over Financial Reporting

In planning and performing my audit of the financial statements, I considered the Municipality's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Municipality's internal control. Accordingly, I do not express an opinion on the effectiveness of the Municipality's internal control.

My consideration of internal control was for the limited purpose described in the preceding paragraph and was not design to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, I identified certain deficiencies in internal control that I consider to be material weaknesses and 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. I consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses. Findings 2013-001, 2013-002, 2013-003 and 2013-006.

INDEPENDENT AUDITOR'S 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)

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. I consider the deficiencies described in the accompany Schedule of Findings and Questioned Costs to be significant deficiencies. Findings 2013-004 and 2013-005.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free from material misstatement, I 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 my audit, and accordingly, I do not express such an opinion. The results of my 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 2013-001, 2013-003 and 2013-006.

Municipality's Response to Findings

Municipality's response to the findings identified in my audit are described in the accompanying Schedule of Findings and Questioned Costs. Municipality's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly I express no opinion on it.

Purpose of this Report

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


Pedro C. Ortiz Ledée, CPA
License Number 5200

Guayama, Puerto Rico
November 16, 2014

Stamp O2698692 was affixed
to the original of this report.



PEDRO C. ORTIZ LEDEE
CERTIFIED PUBLIC ACCOUNTANT

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

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

Report on Compliance for Each Major Federal Program

I 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, 2013. 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.

Management's Responsibility

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

Auditor's Responsibility

My responsibility is to express an opinion on compliance for each of the Municipality's major federal programs based on my audit of the types of compliance requirements referred to above. I conducted my 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 I 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 I considered necessary in the circumstances.

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

Basis for Qualified Opinion on Major Federal Programs

As identified in the findings numbers listed in the table below and described in the accompanying Schedule of Findings and Questioned Costs, the Municipality, did not comply with requirements regarding the following:

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-
133 (CONTINUED)**

Basis for Qualified Opinion on Major Federal Programs (continued)

Awarding Agency	Federal Program	Compliance Requirement	Finding Number
Housing and Urban Development	14.228- CDBG- State's Program	Cash Management	2013-008
Housing and Urban Development	14.228- CDBG- State's Program	Davis-Bacon Act	2013-009
Housing and Urban Development	14.228- CDBG- State's Program	Reporting	2013-010
Housing and Urban Development	14.871- Section 8 Housing Choice Voucher	Eligibility	2013-011
Housing and Urban Development	14.871- Section 8 Housing Choice Voucher	Reporting	2013-012
Housing and Urban Development	14.871- Section 8 Housing Choice Voucher	Special Test- Rolling Forward Equity Balances	2013-013

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

Qualified Opinion on Major Federal Programs

In my opinion, except for the noncompliance described in the "Basis for Qualified Opinion on Major Federal Programs" paragraph, the Municipality, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of the major federal programs listed in the "Basis for Qualified Opinion on Major Federal Programs" paragraph for the year ended June 30, 2013.

Unmodified Opinion on Each of the Other Major Federal Programs

In my opinion, the Municipality complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the other major federal program (Child Care and Development Block Grant) identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs for the year ended June 30, 2013.

Other Matters

The results of my auditing procedures disclosed other instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items 2013-007, 2013-014 and 2013-015. My opinion on each major federal program is not modified with respect to these matters.

Municipality's response to the noncompliance findings identified in my audit are described in the accompanying Schedule of Findings and Questioned Costs. Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly I express no opinion on the response.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-
133 (CONTINUED)**

Report on Internal Control over Compliance

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

My 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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, I identified certain deficiencies in internal control over compliance that I consider to be material weaknesses and 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 a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis. I considered the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2013-008, 2013-009, 2013-010, 2013-011, 2013-012 and 2013-013 to be material weaknesses.

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. I consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2013-007, 2013-014 and 2013-015 to be significant deficiencies.

Municipality's response to the internal control over compliance findings identified in my audit are described in the accompanying Schedule of Findings and Questioned Costs. Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly I express no opinion on the response.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM
AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-
133 (CONTINUED)**

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

PE-C at PE-
Pedro C. Ortiz Ledée, CPA
License Number 5200

Guayama, Puerto Rico
November 16, 2014

Stamp O2698693 was affixed
to the original of this report.



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL
 Schedule of Findings and Questioned Costs
 Fiscal Year Ended June 30, 2013

SECTION I – SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Type of auditor’s report issued on the basic financial statements:

Opinion Units

Governmental activities
 General Fund
 State Legislative Joint Resolutions Fund
 Capital Improvement Bonds Fund
 Debt Service Fund
 Aggregate remaining fund

Type of Opinions

Disclaimer
 Qualified
 Qualified
 Unmodified
 Unmodified
 Qualified

Internal Control over financial reporting:

Material weakness identified?	Yes X	No
Significant deficiencies identified?	Yes X	None 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	None reported

Type of auditor’s report issued on compliance for major programs:

Unqualified opinion for Child Care and Development Block Grant

Qualified opinion for Community Development Block Grants–State’s and Section 8 Housing Choice Voucher Program

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes X	No
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Identification of major programs

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grants – State’s
14.871	Section 8 Housing Choice Voucher Program
93.575	Child Care 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, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-001
REQUIREMENT	ACCOUNTING RECORDS AND REPORTING SYSTEM
CONDITION	The Municipality did not maintain adequate and reliable financial records that generates accurate accounting information for the preparation of the financial statements in conformity with generally accepted accounting principles (GAAP).
CONTEXT	<p>During my examination of the accounting cycle, I noted that the Municipality did not count with complete and accurate accounting records. 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 systems does not provide reliable financial information of transactions related with capital assets, accounts receivables, accounts payables and long-term debts. External consultants summarized in electronic worksheets the revenues, expenditures, capital assets, accounts receivables, accounts payable and long term-debts transactions as part of the process of the financial statement preparation.</p> <p>During the examination of the financial statements, I noted that the General Fund has an unassigned accumulated deficit of \$5,084,702. In addition, the Municipality's General Fund operations resulted in a deficit of \$1,094,363 during the fiscal year 2012-2013.</p> <p>Also, I noted that at June 30, 2013, an obligation of \$459,350, related to the services of waste management was not recorded in the budget liquidation (the manual accounting report that summarizes the annual budgetary operations of the General Fund). This amount was recorded in the financial statements as an account payable at June 30, 2013.</p>
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.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-001 (CONTINUED)
REQUIREMENT	ACCOUNTING RECORDS AND REPORTING SYSTEM
CRITERIA	<p>In addition, Article 8.004 (b) establishes that Municipalities cannot obligate or spend funds, during the fiscal year, in excess of the amounts approved by resolutions or ordinances for the fiscal year. Also, Article 7.010, establishes the procedures and controls over the supervision and compliance with the operational budget. Finally, Article 7.011 (a), states that for any accumulated deficit incurred in the General Fund at the end of any given fiscal year, the Municipality must reserve the necessary financial resources in the General Fund's operating budget of the immediately following fiscal year to cover such deficit.</p>
CAUSE	<p>The Municipality did not maintain effective internal controls over the accounting records from where the financial information is obtain for the preparation of the financial statements in accordance with generally accepted accounting principles. In addition, the Finance Department personnel failed to maintain adequate monitoring procedures over the budgetary process during the fiscal year.</p>
EFFECT	<p>The Municipality is not in compliance with the Articles 7.010, 7.011, 8.004 and 8.010 of the State Act Number 81- <i>Ley de Municipios Autónomos del Estado Libre Asociado de Puerto Rico</i> of August 30, 1991. Also, the Municipality will continue having liquidity problems and will continue affecting the Municipality's ability to finance current operations.</p>
RECOMMENDATION	<p>I recommend management to establish the necessary internal controls and procedures in the Finance Department in order to maintain a complete set of accounting records that provides accurate financial information related to the assets, liabilities, revenues and expenditures. Also, these records should provide trial balances by each fund in the modified accrual basis of accounting. In addition, the records should provide for the maintenance of the capital assets and the general long term debt of the Municipality. In addition, the accounting records of the Municipality should be precisely enough, to support the amounts presented in the financial statements.</p> <p>The Municipality should continue improving its internal controls and procedures over the budgetary process. Also, the Municipality should evaluate a cost reduction plan and continue increasing the collection efforts over the General Fund revenues.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER **2013-001 (CONTINUED)**

REQUIREMENT **ACCOUNTING RECORDS AND REPORTING SYSTEM**

**MANAGEMENT RESPONSE AND
CORRECTIVE ACTION PLAN**

Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain all accounting and financial information and prepare Municipality's financial statements. Such implementation has been made by Rock Solid Technologies, Inc.

Implementation Date: December 31, 2014

Responsible Person: Mrs. Noelia Meléndez Cruz
Finance Department Director (Interim)

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-002
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 lack of an adequate capital assets register did not permit the proper accounting over the capital assets additions, the accumulated depreciation and the depreciation expense presented in the financial statements of the Municipality.
EFFECT	The Municipality is not in compliance with Article 8.010 (c) (3) of the State Law Number 81 of August 30, 1991 and GASB Statement No 34.
RECOMMENDATION	I recommend management and the Property Division of the Municipality to prepare a capital assets inventory and reconcile it with the subsidiary ledger. Also, management should be aware that the accumulated depreciation and the depreciation expense are properly calculated.
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain all accounting and financial information, including a capital assets subsidiary ledger. Such implementation has been made by Rock Solid Technologies, Inc.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER 2013-002 (CONTINUED)

REQUIREMENT ACCOUNTING RECORDS- CAPITAL ASSETS

Also, the Municipality's Finance Department staffs continue updating the capital records. In addition, we are considering engaging with a professional to evaluate the Municipality's infrastructure assets.

Implementation Date: December 31, 2014

Responsible Person: Mrs. Noelia Meléndez Cruz
Finance Department Director (Interim)

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-003
REQUIREMENT	ACCOUNTING RECORDS- INTERFUND TRANSACTIONS
CONDITION	The Municipality transfer funds from the State Legislative Joint Resolutions Fund (a special revenue fund) to the General Fund without adequate supporting documentation.
CONTEXT	<p>During the examination of the accounting records, I noted that during the fiscal year 2012-2013, the Municipality transfer funds to the General Fund bank account, amounting to approximately \$1,115,000, from the State Legislative Joint Resolutions Fund, in which state assignments and grants are accounted. These amounts were pooled with the unrestricted resources of the General Fund. Such state assignments and grants are restricted by Joint Resolutions of both the State House of Representative and Senate.</p> <p>Also, I noted that the Municipality does not maintain adequate internal controls and accurate subsidiary records over the interfund transactions between the General Fund, the State Legislative Joint Resolutions Fund and other non-major funds.</p>
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 General Fund cash resources have been reduced over the past years due to the excess of expenditures over revenues and has caused a liquidity problem to meet the payment of its current obligations and services. This situation caused that the General Fund uses resources from other funds.
EFFECT	The Municipality at this moment did not count with the sufficient resources to comply with the projects or activities for which such funds were obtained and restricted.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF SANTA ISABEL

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER 2013-003 (CONTINUED)

REQUIREMENT ACCOUNTING RECORDS- INTERFUND TRANSACTIONS

RECOMMENDATION The Municipality should either reimburse immediately all resources obtained from the transfers of those funds, or obtain an authorization from the State House of Representative and Senate for the re-program of such funds. The Municipality should continue strengthening its internal controls to avoid subsequent appropriations of other funds whose uses are restricted.

In addition, I recommend management to implement procedures in order to obtain and maintain all the required documentation regarding the interfund transactions.

MANAGEMENT RESPONSE AND
CORRECTIVE ACTION PLAN

Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain all accounting and financial information, including adequate records about interfund transactions. Such implementation has been made by Rock Solid Technologies, Inc. Also, we will transfer the funds mentioned in the Condition form the Current Bank Account to the Special Funds Bank Account as soon as possible.

Implementation Date: December 31, 2014

Responsible Person: Mrs. Noelia Meléndez Cruz
Finance Department Director (Interim)

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-004
REQUIREMENT	ACCOUNTING RECORDS- BANK RECONCILIATIONS AND REVENUES CYCLE
CONDITION	The Municipality does not have effective internal control procedures over the daily collection receipts and the preparation of bank reconciliations.
CONTEXT	<p>During the cash test, I 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. Also, the Model 4a was not prepared on a monthly basis.</p> <p>In addition, during the examination of the revenue cycle of the Municipality, I selected twenty-five (25) collection receipts and noted that the employees of the revenue collection office were preparing the revenue receipts manually. Therefore, these receipts were not accounted in the Municipality's computerized accounting system. Also, the revenue collection office was not preparing the cash receipts for the monthly revenues related to the property taxes and other revenues that were credited to the current bank account through wire transfers.</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. Also, Chapter III, Sections 3, 4 and 5 establishes the procedures and controls to follow regarding the revenues and collection cycle.
CAUSE	The accounting personnel failed to assure that the bank reconciliations were prepared in a complete manner and reconciled with the accounting records. Also, the Municipality did not followed adequate internal controls over the revenues and collection cycle.

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-004 (CONTINUED)
REQUIREMENT	ACCOUNTING RECORDS- BANK RECONCILIATIONS AND REVENUES CYCLE
EFFECT	The Municipality is not in compliance with Chapter III and IV, of the Municipal Administration Regulatory Manual of the OCAM.
RECOMMENDATION	I recommend management to continue improving 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. Also, the revenues collection office of the Municipality should continue improving the internal controls over the collection receipts.

**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.

Also, it's important to comment that actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain all accounting and financial information, including the reconciliation of cash accounts. Such implementation has been made by Rock Solid Technologies, Inc.

Implementation Date: December 31, 2014

Responsible Person: Mrs. Noelia Meléndez Cruz
Finance Department Director (Interim)

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-005
REQUIREMENT	INTERNAL CONTROLS AND PROCEDURES OVER THE DISBURSEMENT CYCLE
CONDITION	During the fiscal year 2012-2013, the Municipality disbursed funds without the appropriate supporting documentation.
CONTEXT	<p>During the examination of the Municipality's disbursement process, I examined forty (40) checks of the General Fund and other non-federal special revenue funds (fifty-nine (59) disbursement vouchers) and noted the following deficiencies:</p> <ol style="list-style-type: none">1. Seven (7) disbursement vouchers, were not approved (signed) by one of the responsible employees;2. In one (1) disbursement voucher the original supplier's invoice was not available for my examination;3. In one (1) disbursement voucher, the receiving report from the supplier was not available for my examination;4. In thirteen (13) disbursement vouchers, the purchase orders were issued after the invoices and the services or goods were received;5. In thirteen (13) disbursement vouchers, I noted that the acquisition process (procurement) was incomplete or was not properly documented by the responsible employees of the acquisition cycle;6. Four (4) disbursement vouchers were not available for my examination.
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.
CAUSE	The Municipality's disbursement procedures and internal controls were not adequately followed by the responsible employees and supervisors.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-005 (CONTINUED)
REQUIREMENT	INTERNAL CONTROLS AND PROCEDURES OVER THE DISBURSEMENT CYCLE
EFFECT	The failure of the application of the disbursement procedures and controls could result in the payment of amounts not properly supported. Also, if the acquisition policies are not followed adequately could result in higher costs of services and goods charged to the Municipality.
RECOMMENDATION	I recommend management to follow and continue improving the internal control procedures in order to obtain and maintain all the required 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: December 31, 2014 Responsible Person: Mrs. Noelia Meléndez Cruz Finance Department Director (Interim)

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION II – FINANCIAL STATEMENTS FINDINGS

FINDING NUMBER	2013-006
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 to the Federal Audit Clearinghouse, in a timely manner, the Single Audit reporting package for the fiscal year ending on June 30, 2013. The due date for this report was no later than March 31, 2014.
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	I 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 2013-2014, which is March 31, 2015. Implementation Date: March 31, 2015 Responsible Person: Mrs. Noelia Meléndez Cruz Finance Department Director (Interim)

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-007
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 the grant disbursement test, I examined five (5) housekeepers' files and noted the following conditions: <ul style="list-style-type: none">a. In the five (5) participant's files, the "Results of Evaluation" sheet were not signed or authorized by the Program's Director;b. The contracts formalized between the Program and the five (5) participants were signed after the services were started;c. In the five (5) participants' files, the monthly follow-up visits were not properly documented, in the worksheets established in the operational guide, to document the visits.
CRITERIA	Code of Federal Regulations 24, 85.20 (a) (2) states that fiscal control and accounting procedures of subgrantees, must be sufficient to permit the tracing of funds to a level of expenditures adequate to establish that funds have not been used in violation of the restrictions and prohibitions of applicable statutes. 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	This situation was caused by the lack of adequate supervision during the selection of the participants' process. Also, the Program's internal controls procedures failed to assure that the required monthly visits and inspections to monitor the services, were properly documented in accordance to the Program's operational guide.
EFFECT	The Program is not in compliance with CFR 24, 85.20 (a) (2) and the operational guide related to the housekeeping services.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-007 (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
RECOMMENDATION	I recommend management to monitor the housekeeping activities to assure that these services commence after the contracts has been approved and signed. In addition, the Program should continue strengthening the internal controls and procedures in order to assure that the follow-up visits are properly documented in accordance with the operational guide.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	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. Implementation Date: December 31, 2014 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, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-008
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 the cash management test, I noted that during the fiscal year 2012-2013, the Program maintained an average adjusted cash balance, in the bank reconciliations, of approximately \$42,480. Also, I examined five (5) requests of funds amounting to \$455,429, made by the Program to the pass-through entity, and found that four (4) of these requests took between ninety-one (91) and two hundred forty-five (245) days from the moment the funds were received and the issuance of the checks. Part of this requests of funds were used to pay other activities of the Program.
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 Program staff 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, 570.489 (c) (1).
RECOMMENDATION	I 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

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-008 (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: December 31, 2014</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, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-009
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	INTERNAL CONTROL
NONCOMPLIANCE	DAVIS-BACON ACT
CONDITION	During the fiscal year 2012-2013, the Program disbursed funds without evaluating the compliance with the Davis-Bacon Act.
CONTEXT	During the grant disbursement test, I noted that during the fiscal year 2012-2013, the Municipality disbursed funds in the amount of \$23,496, for the construction project “Rehabilitación Casa Alcaldía” and I did not found evidence that the contractor submitted the weekly payrolls to the Program.
CRITERIA	Davis- Bacon Act, 42 USC 5310.
CAUSE	The Municipality failed to apply all the monitoring procedures developed to test applicable contractors with respect to the payment of prevailing wages.
EFFECT	The Municipality is not in compliance with Davis- Bacon Act, 42 USC 5310.
RECOMMENDATION	I recommended management to continue improving the existing controls in order to assure that the contractors submit to the Program all the weekly payrolls.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	We will give instructions to the responsible employee to collect from the contractors the weekly payrolls and verify that wages paid are in accordance with rates established by the US Department of Labor. Implementation Date: December 31, 2014 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, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-010
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	<p>During the reporting test, I 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 an adequate accounting system.</p> <p>Also, I found that the accumulative expenditures reported in the quarterly reports of the fiscal year 2012-2013, submitted to the pass-through entity (OCAM), did not reconcile with the accounting records (check register) for the net amount of \$80,747.</p> <p>Finally, the cash balance at June 30, 2013, reported in the quarterly reports, per program years, did not agree with the bank reconciliation for the amount of \$492,658.</p>
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 accounting staff is not reconciling its accounting records and bank reconciliations with the quarterly reports in order to assure that there are no differences.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-010 (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 the financial information submitted to the pass-through entity in its quarterly reports agrees with the accounting records.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain accurate accounting and financial information. 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. Implementation Date: December 31, 2014 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-011
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 the eligibility test, I examined fifteen (15) participant's files, and noted the following conditions:</p> <ul style="list-style-type: none">a. In three (3) participants' files, the Enterprise Income Verification (EIV) was not available for examination. In addition, in one (1) participant's file the EIV was issued after the contract formalization;b. In three (3) participant's files, I noted that a member 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, I 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 one (1) participant's file, the Penal Record Certificate for one family member was not available for my examination, and was not included as part of the file documentation;d. In two (2) participants' files, I noted that the Program calculated a deduction for two (2) dependents older than eighteen (18) years and I did not found evidence that demonstrated that the members were students or disables.
CRITERIA	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.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-011 (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	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.
CAUSE	The Program's internal controls failed to assure that the EIV System was used during the mandatory annual and interim reexamination as a third party income verification of the family income. In addition, the Program's staff failed to obtain all the required documentation necessary for the reexamination process.
EFFECT	The Program is not in compliance with Code of Federal Regulation 24, Section 982.516 (a) (1), (2) and (g).
RECOMMENDATION	I recommend management to continue strengthening the internal controls and procedures designed to verify the family income and composition using third parties information and the EIV system in each mandatory reexamination of the participants. Also, the Program should obtain all the necessary information related to the income and family composition of the participant's during the reexamination process. Finally, the Program should be aware that all heads of household and members 18 years or older must signed the release of information during the reexamination process.
QUESTIONED COSTS	None

**COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-011 (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
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	The 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. Also, the Program Coordination have been instructed to strength the established internal control and procedures in order to obtain all the necessary information related to the income and family composition of the participant's during the reexamination process, and to be aware that all heads of household and family members 18 years or older sign the release of information during the reexamination process.

Implementation Date: December 31, 2014

Responsible Person: Mr. Ricardo Burgos Colón
Federal Programs Director

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-012
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 the reporting test, I 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, expenditures and equities of the Program, in an adequate accounting system.</p> <p>Also, I found that the accumulative HAP and administrative expenditures reported monthly in the Voucher Management System (VMS) have differences of approximately \$2,149 and \$8,591, respectively, with the accounting records (check register) of the Program.</p> <p>In addition, the amounts of Administrative Fee Equity and HAP Equity reported at June, 30, 2013, in the VMS were not adequately supported with accurate accounting records.</p> <p>Finally, the Municipality failed to submit, in a timely manner, the unaudited and audited financial information of the Program for the fiscal year 2012-2013 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, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-012 (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 electronically, the unaudited and audited reports.
EFFECT	The Program did not submit accurate monthly reports to HUD in order to comply with the Federal regulations.
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. Also, the Program should comply with the requirement established by HUD, to submit electronically the unaudited and audited financial information of the Program.
QUESTIONED COSTS	None
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain accurate accounting and financial information. Also, we will submit, in a timely manner, the audited information of the Program, for the fiscal year 2014-2015, through the FASS-PH system. Implementation Date: December 31, 2014 Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-013
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 accounting over the roll-forward equity balances.
CONTEXT	During the examination of the accounting records, I 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 equities reported in the Voucher Management System (VMS) during the fiscal year 2012-2013 were not traceable to the accounting records, and were not properly supported with adequate documentation.
CRITERIA	Code of Federal Regulations 24, 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 equities 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	I recommended management to prepare an analysis, supported by adequate accounting records, of the HAP and the administrative fee equities accounts and adjust or correct any errors on these accounts.

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-013 (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**

Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain accurate accounting and financial information. Also, we will prepare an analysis of the Administrative and HAP equities and made the necessary adjustments to reflect the corrected balances.

Implementation Date: December 31, 2014

Responsible Person: Mr. Ricardo Burgos Colón
Federal Programs Director

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-014
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 the evaluation, I 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, Section 982.156 (a) and (c).
RECOMMENDATION	I 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
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>In November 2014, we have entered into a depository agreement, in the form required by HUD, with our financial institution.</p> <p>Implementation Date: Actually implemented</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

COMMONWEALTH OF PUERTO RICO
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SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-015
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 over the parents' contributions.
CONTEXT	During the examination of the accounting records of the Program, I noted that there were not adequate controls over the billing, receipts and deposits of the parents' contributions for the Child Care services.
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. 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 parents' contributions transactions.
EFFECT	The Program is not in compliance with CFR 45, Part 92.20 (b) (2) and the Contract with the pass-through agency.
RECOMMENDATION	I recommend management to implement adequate procedures to ensure that the financial transactions related to the parents' contributions are properly recorded as part of 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, 2013

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING NUMBER	2013-015 (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
MANAGEMENT RESPONSE AND CORRECTIVE ACTION PLAN	<p>Actually, the Municipality is in the implementation process of a new accounting software (SIMA, by its acronyms in Spanish) in order to maintain accurate accounting and financial information, including the presentation of 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: December 31, 2014</p> <p>Responsible Person: Mr. Ricardo Burgos Colón Federal Programs Director</p>

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
12-III-08	Allowable Activities-Housekeeping Services	14.228	None	No corrective action has been taken. Finding Reference 2013-007.
12-III-09	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 2013-008.
12-III-10	Equipment and Real Property Management	14.228	None	Full corrective action was taken.
12-III-11	Procurement, Suspension and Debarment	14.228	None	Full corrective action was taken.
12-III-12	Reporting	14.228	None	No corrective action has been taken. Finding Reference 2013-010.
12-III-13	Allowable Cost-Disbursement Process	14.871	None	The auditors did not identified during fiscal year 2012-2013 transactions related to this finding.
12-III-14	Allowable Activities-Segregation of Duties	14.871	None	Full corrective action was taken.
12-III-15	Eligibility	14.871	None	No corrective action has been taken. Finding Reference 2013-011.
12-III-16	Reporting	14.871	None	No corrective action has been taken. Finding Reference 2013-012.
12-III-17	Special Test-Reasonable Rent	14.871	None	Full corrective action was taken.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
12-III-18	Special Test-HQS	14.871	None	Full corrective action was taken.
12-III-19	Special Test-HAP Register	14.871	None	Full corrective action was taken.
12-III-20	Special Test-Rolling Forward Equity Balances	14.871	None	No corrective action has been taken. Finding Reference 2013-013.
12-III-21	Special Test-Depository Agreement	14.871	None	No corrective action has been taken. Finding Reference 2013-014.
12-III-22	Eligibility	93.575	None	Full corrective action was taken.
12-III-23	Equipment and Real Property Management	93.575	None	Full corrective action was taken.
12-III-24	Program Income	93.575	None	No corrective action has been taken. Finding Reference 2013-015.
12-III-25	Reporting	93.575	None	No corrective action has been taken. Finding Reference 2013-015.
11-III-07	Allowable Activities-Housekeeping Services	14.228	None	No corrective action has been taken. Finding Reference 2013-007.
11-III-08	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 2013-08.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-10	Equipment and Real Property Management	14.228	None	Full corrective action was taken.
11-III-11	Reporting	14.228	None	No corrective action has been taken. Finding Reference 2013-010.
11-III-12	Allowable Cost-Disbursement Process	14.871	\$10,380	The auditors did not identified during fiscal year 2012-2013 transactions related to this finding.
11-III-13	Allowable Activities-Segregation of Duties	14.871	None	Full corrective action was taken.
11-III-14	Eligibility	14.871	None	No corrective action has been taken. Finding Reference 2013-011.
11-III-15	Reporting	14.871	None	No corrective action has been taken. Finding Reference 2013-012.
11-III-17	Special Test-Reasonable Rent	14.871	None	Full corrective action was taken.
11-III-19	Special Test-Housing Assistance Payment Register	14.871	None	Full corrective action was taken.
11-III-20	Special Test-Rolling Forward Equity Balances	14.871	None	No corrective action has been taken. Finding Reference 2013-013.
11-III-21	Special Test-Depository Agreement	14.871	None	No corrective action has been taken. Finding Reference 2013-014.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
11-III-22	Equipment and Real Property Management	93.575	None	Full corrective action was taken.
11-III-23	Program Income	93.575	None	No corrective action has been taken. Finding Reference 2013-015.
11-III-24	Reporting	93.575	None	No corrective action has been taken. Finding Reference 2013-015.
11-III-25	Procurement, Suspension and Debarment	93.713	None	No corrective action has been taken. The auditors did not identified during fiscal year 2012-2013 transactions related to this finding.
10-06	Reporting- Fiscal Requirements	14.228	None	No corrective action has been taken. Finding Reference 2013-010.
10-07	Reporting	14.228	None	No corrective action has been taken. Finding Reference 2013-010.
10-08	Equipment and Real Property Management	14.228	None	Full corrective action was taken.
10-09	Cash Management	14.228	None	No corrective action has been taken. Finding Reference 2013-008.
10-11	Special Test-Housekeepers Project	14.228	None	No corrective action has been taken. Finding Reference 2013-007.
10-12	Reporting- Fiscal Requirements	14.871	None	No corrective action has been taken. Finding Reference 2013-012.

**COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
10-13	Activities Allowed- Segregation of Duties	14.871	None	Full corrective action was taken.
10-15	Eligibility	14.871	None	No corrective action has been taken. Finding Reference 2013-011.
10-16	Special Test- HAP Register	14.871	None	Full corrective action was taken.
10-18	Special Test- Depository Agreement	14.871	None	No corrective action has been taken. Finding Reference 2013-014.
10-19	Reporting- Fiscal Requirements	93.575	None	No corrective action has been taken. Finding Reference 2013-015.
10-20	Program Income	93.575	None	No corrective action has been taken. Finding Reference 2013-015.
10-21	Equipment and Real Property Management	93.575	None	Full corrective action was taken.
09-04	Reporting	14.228	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
09-05	Equipment and Real Property Management	14.228	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
09-06	Reporting- Fiscal Requirements	14.228	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
09-08	Reporting- Fiscal Requirements	14.871	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
09-09	Reporting- Fiscal Requirements	93.575	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
09-10	Program Income	93.575	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
09-11	Equipment and Real Property Management	93.575	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
08-04	Equipment and Real Property Management	14.228	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
08-08	Reporting	93.575	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
08-09	Program Income	93.575	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
08-10	Equipment and Real Property Management	93.575	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.
07-06	Equipment and Real Property Management	14.228	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

FOR THE FISCAL YEAR ENDED JUNE 30, 2013

FINDING NUMBER	COMPLIANCE	CFDA NUMBER	QUESTIONED COSTS	AUDITEE COMMENTS
06-06	Equipment and Real Property Management	14.228	None	Finding no longer valid. The audit finding does not warrant further action because more than two years have passed since the audit report in which the finding occurred was submitted to the Federal clearinghouse.